TRANSCRIPT OF RECORD

IN THE

United States Court of Appeals

FIFTH CIRCUIT

No. 16,373

UNITED STATES OF AMERICA

Appellant

versus

MERRY BROTHERS BRICK AND TILE COMPANY

Appellee

Appeal from the United States District Court for the Southern District of Georgia

UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF GEORGIA
AUGUSTA DIVISION

MERRY BROTHERS BRICK AND TILE COMPANY,
Plaintiff,

vs. CIVIL ACTION NO. 752

UNITED STATES OF AMERICA,
Defendant.

COMPLAINT

1

1. Plaintiff brings this action against defendant pursuant to Section 1346 (a) (1) of Title 28 of the United States Code, Act of June 25, 1948, c. 646, 62 Stat. 869, 933, as amended by the Act of July 30, 1954, C.648, 1, 68 Stat. 589.

2. This action is brought for the recovery of $61,419.01 of income tax, $51,630.77 of excess profits tax and $21,574.56 of interest collected from plaintiff for the calendar year 1951, also, for the recovery of $61,763.12 of income tax, $8,151.10 of excess profits tax and $9,835.31 of interest collected from plaintiff for the calendar year 1952, also for the recovery of $65,351.15 of income tax and $1,823.32 of interest collected from plaintiff for the calendar year 1953, and for the recovery of $68,383.69 of income tax and $301.33 of interest collected from plaintiff for the calendar year 1954, and interest on said sums from the respective dates of payment.

3. Plaintiff is a corporation incorporated and doing business under the laws of the State of Georgia, with its principal

place of business at Augusta, Georgia, within this District and Division.

4. Plaintiff keeps its books on the accrual basis method of accounting and reports its income on a calendar year basis.

5. Within the time prescribed by law, plaintiff made and filed its income tax return and its excess profits tax return for the calendar year 1951, showing an income tax liability and an excess profits tax liability. As the result of an examination by a Revenue Agent of its returns for 1951 and its returns for 1952, plaintiff's income tax liability for 1951 was adjusted to $230,118.56 and its excess profits tax liability was adjusted to $54,630.77. If plaintiff is entitled to deductions for depletion for 1951 and 1952, as hereinafter alleged, then, by reason thereof, plaintiff has an excess profits tax credit from 1952 which plaintiff is entitled to carry back to 1951. Such carry-back credit was claimed and applied by plaintiff with respect to its excess profits tax liability for 1951, as the result of which the excess profits tax liability shown on plaintiff's return for 1951 was extinguished.

6. Plaintiff's income tax liability for 1951, as adjusted, was paid on the following dates, to-wit:

$80,425.00 on February 20, 1952
$75.00 on February 28, 1952
$78,184.83 on June 13, 1952
$34,218.18 on September 13, 1952
$34,218.18 on December 13, 1952
$5,306.10 on October 11, 1954.

7. On its returns for 1951, plaintiff claimed a deduction for percentage depletion in the amount of $145,583.30 on its

deposit of brick and tile clay. Such depletion was computed on the basis of and represents 5% of the selling price of plaintiff's burnt brick and tile for 1951, f.o.b. plant, loaded for shipment.

8. Within the time prescribed by law, plaintiff also made and filed its income tax return for the calendar year 1952 showing an income tax liability and no excess profits tax liability. As the result of an examination by a Revenue Agent of its return for 1952, plaintiff's income tax liability was adjusted to $165,264.28, and its excess profits tax liability was shown to be $8,151.10.

9. Plaintiff's income tax liability and excess profits tax liability for 1952, as adjusted, was paid as follows:

$61,488.14 on March 15, 1953
$61,488.14 on June 12, 1953
$15,372.04 on September 15, 1953
$15,372.03 on December 14, 1953
$71,543.93 on October 11, 1954

10. On its return for 1952, plaintiff claimed a deduction of $140,616.98 as percentage depletion on its deposit of brick and tile clay. Such depletion was computed on the basis of and represents 5% of the selling price of plaintiff's burnt brick and tile for 1952, f.o.b. plant, loaded for shipment.

11. Within the time prescribed by law, plaintiff made and filed its income tax return for the calendar year 1953 showing an income tax liability and no excess profits tax liability. As the result of an examination by a Revenue Agent of its return for 1953, plaintiff's income tax liability was adjusted to $152,237.94.

12. Plaintiff's income tax liability for 1953, as adjusted, was paid as follows:

$63,295.92 on March 15, 1954
$63,295.92 on June 11, 1954
$ 7,032.88 on September 13, 1954
$11,380.34 on October 11, 1954
$ 7,032.88 on December 13, 1954.

13. On its return for 1953, plaintiff claimed a deduction of $142,392.14 as percentage depletion on its deposit of brick and tile clay. The depletion taken was computed on the basis of and represents 5% of the selling price of claimant's burnt brick and tile for 1953, f.o.b. plant, loaded for shipment.

14. The Commissioner of Internal Revenue, hereinafter sometimes referred to as the Commissioner, caused the aforesaid income tax returns of plaintiff for the calendar years 1951, 1952 and 1953 to be examined and a Revenue Agent's report, dated October 8, 1954, stating the result of such examination, was transmitted to plaintiff under date of June 6, 1955. Such report allowed plaintiff a deduction for percentage depletion on the basis set forth in paragraph 17 hereof, which deduction for each of said years was less than the deduction computed on the selling price of the burnt brick and tile which plaintiff claimed.

15. As a result of the decrease in the percentage depletion allowed in such report for 1952, the unused excess profits tax credit of plaintiff from that year which was carried back to 1951, as alleged in paragraph 5 hereof, was extinguished and lost to plaintiff. Consequently, said report showed plaintiff liable for excess profits tax for 1951 in the amount of $54,630.77, and for 1952 in the amount of $8,131.10.

16. Such Revenue Agent's report proposed deficiencies in income tax and excess profits tax for 1951 and for 1952, and in income tax for 1953, on the basis that the deductions for depletion which plaintiff had taken on its returns for those years, respectively, were excessive. Other adjustments in said report, not relating to depletion, were agreed to by plaintiff.

17. The deduction which the Commissioner allowed plaintiff for percentage depletion in accordance with said Revenue Agent's report referred to in paragraph 14 hereof was computed by allocating to what the Agent's report terms "mining" a proportionate part of plaintiff's costs and allocating the rest of such costs to what the Agent's report terms "manufacturing".

18. On May 21, 1955, plaintiff executed Treasury Department Form 870 waiving restrictions on the assessment and collection of the deficiencies proposed, and deficiencies were assessed under date of June 8, 1955, as follows:

For 1951—Income tax and excess profits tax $121,017.18, interest $23,389.78, less 10-13-54 Uncl: $5,306.10—
Balance $139,130.86.

For 1952—Income tax and excess profits tax $81,158.15, interest $10,923.60, less 10-13-54 Uncl. $11,543.93—
Balance $83,837.82.

For 1953—Income tax and excess profits tax $76,931.49, interest $5,228.63, less 10-13-54 Uncl. $11,580.34—
Balance $70,579.78.

19. Plaintiff paid such asserted deficiencies on July 1, 1955.

20. Within the time prescribed by law, plaintiff made and filed its income tax return for the calendar year 1954 showing an income tax liability of $238,043.38, including interest of $301.33.

21. On such return for 1954, plaintiff claimed a deduction of $18,803.91 as percentage depletion on its deposit of brick and tile clay. Such depletion was computed on the basis of 5% of 12.51% of the selling price of claimant's burnt brick and tile for 1954, f.o.b. plant, loaded for shipment, which is the same basis on which the Commissioner allowed plaintiff percentage depletion for 1951, 1952 and 1953, in accordance with said Revenue Agent's report.

22. The income tax liability shown on such return for 1954 was paid as follows:

$105,117.63 on March 15, 1955
$132,691.42 on June 14, 1955
$301.33 interest, on June 14, 1955

23. On July 22, 1955, plaintiff duly filed with the District Director of Internal Revenue in Atlanta, claims for refund of income tax and excess profits tax and interest thereon paid pursuant to such additional assessments, as follows:

For 1951 — Income tax of $61,119.04, excess profits tax of $51,630.77 and interest of $21,574.56.

For 1952 — Income tax of $64,763.12, excess profits tax of $8,151.10 and interest of $9,835.31.

For 1953 income tax of $65,351.15 and interest of $1,823.32.

Such claims for refund were filed on the ground that, under Section 114 of the Internal Revenue Code of 1939 plaintiff is entitled to a percentage depletion deduction on its deposit of brick and tile clays and had correctly computed the same on the selling price, f.o.b. plant, loaded for shipment, of the burnt brick and tile which it produces. Such deduction is greater for each year than the deduction allowed by said Revenue Agent's report for that year. Said claims for refund set forth the grounds and reasons upon which this suit is brought.

24. On July 22, 1955, plaintiff also duly filed with the District Director of the Internal Revenue in Atlanta a claim for refund of income tax for 1954 in the amount of $68,383.69, and interest paid in the amount of $501.83, on the ground that, under Section 611 of the Internal Revenue Code of 1954, plaintiff is entitled to a percentage depletion deduction on its deposit of brick and tile clay computed on the selling price, f.o.b. plant, loaded for shipment, of the brick and tile which it produces. Such deduction is greater than the deduction claimed by plaintiff in the return which it filed for 1954. Such claim for refund set forth the grounds and reasons upon which this suit is brought.

25. On November 17, 1955, plaintiff's said claims for refund for 1951, 1952, 1953 and 1954, were denied and on November 17, 1955, the Commissioner, under Section 3772 (a) (2) of the Internal Revenue Code of 1939, and under Section 6532 (a) (1) of the Revenue Code of 1954, mailed by Registered Mail a notice of the disallowance of such claims for refund.

26. If plaintiff is entitled to deductions for depletion as alleged in paragraphs 36, 38, 40 and 43 hereof, for 1951, 1952, 1953 and 1954, respectively, plaintiff has overpaid its income and excess profits tax for 1951 in the respective amount shown on the claim for refund with respect to that year referred to in paragraph 23 hereof, has overpaid its income and excess profits tax for 1952 in the respective amounts shown on the claim for refund with respect to that year referred to in paragraph 23 hereof, has ovepaid its income tax for 1953 in the amount shown on the claim for refund with respect to that year referred to in paragraph 23 hereof, and has overpaid its income tax for 1954 in the amount shown on the claim for refund referred to in paragraph 24 hereof.

27. Plaintiff owns and operates several clay pits located in Richmond County, Georgia, near Augusta. It is engaged in the business of mining clay from these pits and making brick and tile from such clay in two brick and tile plants which are located near the clay pits.

28. Section 23(m) of the Internal Revenue Code of 1939, applicable to the years 1951, 1952 and 1953, and Section 611(a) of the Internal Revenue Code of 1954, provide for a deduction in computing net income of an allowance for depletion of "mines, oil and gas wells, other natural deposits and timber". Section 114 (b) (4) (A) of the Code of 1939 and Section 613(b)(5)(A) of the Code of 1954 provide that the allowance for depletion under Section 23(m) of the Code of 1939 and under Section 611 of the Code of 1954 in the case of "brick and tile clay" shall be five per centum of the "gross income from the property during the taxable year", but not to exceed fifty per centum of the taxpayer's net income from the property, computed without allowance for depletion.)

29. The term "gross income from the property" as used in Section 114(b)(4)(A) of the Code of 1939 is defined in Section 114(b)(4)(B) of that Code, which states that "gross income from the property" means the gross income from mining; also that the term "mining" as used therein shall be considered to include not merely the extraction of the ores or minerals from the ground, but also the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products . . ." These same definitions and provisions are contained in Section 613(c)(1) and Section 613(c)(2) of the Code of 1954, respectively.

30. There is no clay which by its physical or chemical characteristics can be identified as being only brick and tile clay. The term "brick and tile clay" as used in Section 114(b)(4)(A) of the Code of 1939 and Section 613(b)(5)(A) of the Code of 1954 means clay which is in fact used or for use in the production of common brick and tile and kindred products, and does not include clay used for any other purpose.

31. The Treasury allows a deduction for depletion of "brick and tile clay" on a percentage basis under Section 114(b)(4)(A) of the Code of 1939 and Section 613(b)(5)(A) of the Code of 1954 only for clay used or for use in the production of common brick and tile and kindred products. Section 29.23(m)—5(b) of Treasury Regulations 118 defines "clay brick and tile" as follows:

> "Clay used or sold for use in the manufacture of common brick, drain and roofing tile, sewer pipe, flower pots and kindred products (other than clay specifically identified as clay for which a 15% rate of percentage depletion is provided)."

32. Plaintiff sells all of the clay which it mines in the form of burnt brick and tile, except for negligible amounts of raw clay, none of which is sold for use in the making of common brick and tile or kindred products.

33. As such clay is defined in paragraphs 30 and 31 hereof, there is no market for the brick and tile clay mined by plaintiff before it is put in the form of burnt brick and tile.

34. Of the brick and tile clay mined in the United States there is opportunity for the sale of only a negligible quantity before it is put in the form of burnt brick and tile.

35. The following are the processes applied by plaintiff to the raw clay in order to put it in the form of burnt brick and tile:

(a) The clay is mined at several different pits simultaneously by draglines and loaded in dump cars which operate on railroad tracks and carry the clay to the plant.

(b) The clay is dumped from the cars into large feeders which mix the clay and reduce the large chunks to a size that can be carried on a conveyor belt.

(c) The clay mined from the several different pits is discharged from the feeders on conveyor belts which carry it first to a disintegrator or crusher and then to a storage shed, where it is blended and weathered.

(d) The clay blended and weathered in the storage shed is then loaded onto a conveyor belt which carries the clay to a set of smooth roll crushers, which further reduce the size of the chunks. In one of the plants there are two small additional granulators or pug mills, through which the clay passes before reaching the smooth roll crushers.

(e) From these smooth roll crushers the clay is discharged onto another conveyor belt which carries it by belt conveyors to another feeder where the clay is further blended or mixed.

(f) From the feeder the clay is discharged into the pug mill, which is a part of the brick machine wherein water is added as the final tempering process.

(g) From the pug mill the clay passes through a sealing die into and through a vacuum chamber where air is evacuated from the clay by a vacuum pump. The clay then falls into the extrusion section of the machine, where it is forced under pressure through various shapes of dies in long ribbons.

(h) The long ribbons of clay as extruded through the dies pass into the cutting machine, which cuts them into clay units of the desired size or length.

(i) The clay units as cut pass onto a conveyor belt and are then stacked by hand on dryer cars. These cars of brick are then moved to the dryer tunnels, where free water is evaporated from the clay units by warm air from fans which is blown on and over the units.

(j) When the free water is thus removed, the clay units are stacked either in periodic kilns, semi-continuous kilns, or continuous tunnel kilns.

(k) The clay units are then burned, either in periodic, semi-continuous or continuous tunnel kilns.

(l) The burnt brick and tile are then removed from the kilns.

(m) After they have been removed from the kilns, the burnt brick and tile are loaded for shipment to purchasers.

36. In the claim for refund for 1951, referred to in paragraph 23 hereof, plaintiff claimed that it is entitled to a deduction for 1951 in the amount of $145,583.30 as percentage depletion on its clay deposit under the percentage depletion method provided by Section 114(b)(4)(A) of the Revenue Code of 1939. Five percent (5%) of plaintiff's net sales for 1951 of burnt brick and tile produced by it, f.o.b. plant, loaded for shipment, is $145,583.30. Such amount is less than 50% of the net income from such sales.

37. The percentage of plaintiff's total costs which the Commissioner allocated to what said Revenue Agent's report terms "mining", as distinguished from "manufacturing", computed as alleged in paragraph 17 hereof, was 12.81% for 1951. The Commissioner applied this percentage to the sales of burnt brick and tile and allowed a 5% depletion deduction computed on such figure. By this method, he computed the deduction for 1951 to be $18,649.22.

38. In the claim for refund for 1952, referred to in paragraph 23 hereof, plaintiff claimed that it is entitled to a deduction for 1952 in the amount of $140,616.98 as percentage depletion on its clay deposit under the percentage depletion method provided by Section 114(b)(4)(A) of the Revenue Code of 1939. Five percent (5%) of plaintiff's net sales for 1952 of burnt brick and tile produced by it, f.o.b. plant, loaded for shipment, is $140,616.98. Such amount is less than 50% of the net income from such sales.

39. The percentage of plaintiff's total costs which the Commissioner allocated to what said Revenue Agent's report terms "mining", as distinguished from "manufacturing", computed as alleged in paragraph 17 hereof, was 11.43% for

1952. The Commissioner applied this percentage to the sales of burnt brick and tile and allowed a 5% depletion deduction computed on such figure. By this method, he computed the deduction for 1952 to be $16,072.52.

40. In the claim for refund for 1953, referred to in paragraph 23 hereof, plaintiff claimed that it is entitled to a deduction for 1953 in the amount of $142,392.14 as percentage depletion on its clay deposit under the percentage depletion method provided by Section 114(b)(4)(A) of the Revenue Code of 1939. Five percent (5%) of plaintiff's net sales for 1953 of burnt brick and tile produced by it, f.o.b. plant, loaded for shipment, is $142,392.14. Such amount is less than 50% of the net income from such sales.

41. The percentage of plaintiff's total costs which the Commissioner allocated to what said Revenue Agent's report terms "mining", as distinguished from "manufacturing", computed as alleged in paragraph 17 hereof, was 11.74% for 1953. The Commissioner applied this percentage to the sales of burnt brick and tile and allowed a 5% depletion deduction computed on such figure. By this method, he computed the deduction for 1953 to be $16,716.84.

42. In its return for 1954, plaintiff claimed a deduction for percentage depletion of $18,803.91. Such deduction was computed by allocating to what the Revenue Agent's report, referred to in paragraph 14 hereof, terms "mining" a proportionate part of plaintiff's costs and allocating the rest of said costs to what the Agent's report terms "manufacturing". The percentage of total costs allocated to what the Agent's report terms "mining" was 12.51%. Plaintiff applied this percentage to the sales of burnt brick and tile and took a 5% depletion based

on such figure. By this method plaintiff computed such deduction to be $33,803.91.

43. In the claim for refund for 1954, referred to in paragraph 24 hereof, plaintiff claimed that it is entitled to a deduction for 1954 in the amount of $150,311.00 as depletion on its clay deposit under the percentage depletion method provided by Section 613(b)(5)(A) of the Revenue Code of 1954. Five percent (5%) of plaintiff's net sales for 1954 of burnt brick and tile produced by it, f.o.b. plant, loaded for shipment, is $150,311.00. Such amount is less than 50% of the net income from such sales.

44. The processes listed and described in paragraph 35 hereof are the ordinary ones by which brick and tile clay generally is extracted from the ground and processed into brick and tile.

45. In the case of brick and tile clay, burnt brick and tile are "the commercially marketable mineral product or products" as that term is used in Section 114(b)(4)(B) of the Internal Revenue Code of 1939, and in Section 613(c)(2) of the Internal Revenue Code of 1954, and the processes described in paragraph 35 hereof are, within the meaning of those Sections, the "ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products."

46. Plaintiff was entitled to a percentage depletion deduction for 1951 of $145,583.30. All the income attributable to extracting the clay from the ground and to the processes applied to produce the burnt brick and tile is properly income from "mining" and thus "gross income from the property" as

those terms are defined in Section 114(b)(4)(B) of the Code of 1939.

47. The action of the Commissioner in excluding from "mining" a part of the ordinary treatment process applied by plaintiff to produce burnt brick and tile, thus excluding from "gross income from the property" the income attributable to such processes and in limiting plaintiff's deduction for percentage depletion to $18,649.22 for 1951, was erroneous, illegal and without warrant in law.

48. Plaintiff was entitled to a percentage depletion deduction for 1952 of $140,616.98. All the income attributable to extracting the clay from the ground and to the processes applied to produce the burnt brick and tile is properly income from "mining" and thus "gross income from the property" as those terms are defined in Section 114(b)(4)(B) of the Code of 1939.

49. The action of the Commissioner in excluding from "mining" a part of the ordinary treatment process applied by plaintiff to produce burnt brick and tile, thus excluding from "gross income from the property" the income attributable to such processes, and in limiting plaintiff's deduction for percentage depletion to $16,072.52 for 1952, was erroneous, illegal and without warrant in law.

50. Plaintiff was entitled to a percentage depletion deduction for 1953 of $142,392.14. All the income attributable to extracting the clay from the ground and to the processes applied to produce the burnt brick and tile is properly income from "mining" and thus "gross income from the property" as those terms are defined in Section 114(b)(4)(B) of the Code of 1939.

51. The action of the Commissioner in excluding from "mining" a part of the ordinary treatment process applied by plaintiff to produce burnt brick and tile, thus excluding from "gross income from the property" the income attributable to such processes, and in limiting plaintiff's deduction for percentage depletion to $16,716.84 for 1953, was erroneous, illegal and without warrant in law.

52. Plaintiff was entitled to a percentage depletion deduction for 1954 of $150,311.00. All the income attributable to extracting the clay from the ground and to the processes applied to produce the burnt brick and tile is properly income from "mining" and thus "gross income from the property", as those terms are defined in Section 613(c)(2) of the Internal Revenue Code of 1954.

53. In deducting as percentage depletion on its return for 1954 the sum of $13,303.91, plaintiff thereby excluded from "mining" a part of the ordinary treatment processes applied by plaintiff to produce burnt brick and tile, thus excluding from "gross income from the property" the income attributable to such processes, and plaintiff's action in so doing was erroneous and illegal.

54. By reason of the facts set forth in this complaint, there is now due and owing from defendant to plaintiff the sum of $362,136.39, with interest theron as provided by law, from the dates of payment thereof. Of said sum $140,624.37 was erroneously and illegally assessed against and collected from plaintiff as income tax, excess profits tax and interest thereon for 1951, $82,749.53 was erroneously and illegally assessed against and collected from plaintiff as income tax, excess profits tax and interest thereon for 1952, $70,174.17 was er-

roneously and illegally assessed against and collected from plaintiff as income tax and interest thereon for 1953, and $63,888.02 was erroneously and illegally collected from plaintiff as income tax and interest thereon for 1954.

55. Although repayment thereof has been demanded, no part of the sum of $362,436.39 has been credited, remitted, refunded, or repaid to the plaintiff or to anyone on its account.

WHEREFORE, plaintiff prays judgment against defendant in the principal sum of $362,436.39, and interest thereon as provided by law from the dates of payment hereinabove specified, together with costs, and such other and further relief as to the Court seems meet and proper.

Fulcher, Fulcher, & Flagler,
W. M. FULCHER,
Counsel for Plaintiff.

410 Marion Building
Augusta, Georgia

U. S. District Court
Augusta Division
Filed in Office
November 21, 1955
Jesse Baldwin
Deputy Clerk

UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF GEORGIA
AUGUSTA DIVISION

MERRY BROTHERS BRICK AND TILE COMPANY
Plaintiff

v. Civil Action File No. 752

UNITED STATES OF AMERICA
Defendant

SUMMONS

To the above named Defendant:

You are hereby summoned and required to serve upon

Fulcher, Fulcher & Hagler

plaintiff's attorney, whose address

410 Marion Building, Augusta, Georgia

an answer to the complaint which is herewith served upon you, within 60 days after service of this summons upon you, exclusive of the day of service. If you fail to do so, judgment by default will be taken against you for the relief demanded in that complaint.

EUGENE F. EDWARDS
Clerk of Court
JESSE BALDWIN
Deputy Clerk

Date: November 21, 1955

RETURN ON SERVICE OF WRIT

I hereby certify and return, that on the 7th day of December 1955, I received this summons and served it together with the complaint herein as follows: By handing to and leaving with William C. Calhoun; United States Attorney, a copy, at Augusta, Georgia on December 7, 1955 and mailed a copy to The Attorney General, Washington, D. C. by Registered Mail and also a copy to the Commissioner of Internal Revenue, Washington, D. C. by Registered Mail, on December 8, 1955.

U. S. District Court
Augusta Division
Filed in Office
Dec. 12, 1955
ORLENA T. WEAVER
Deputy Clerk
J. F. BROPHY
United States Marshal
By: RALPH M. TEMPLES
Deputy U. S. Marshal

IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF GEORGIA
AUGUSTA DIVISION

MERRY BROTHERS BRICK AND TILE COMPANY, Plaintiff v. UNITED STATES OF AMERICA, Defendant.	CIVIL ACTION NO. 752

ANSWER

Comes now the United States, by its Attorney, William C. Calhoun, United States Attorney for the Southern District of Georgia, and answers the allegations of the complaint as follows:

1. The allegations of paragraphs numbered 1, 2, 3, and 4 are admitted.

5. The allegations of paragraph numbered 5 are denied, except it is admitted that plaintiff timely made and filed its income tax return and excess profits tax return for the calendar year 1951, showing an income tax liability and an excess profit tax liability; and that as the result of an examination by a Revenue Agent of plaintiff's returns for 1951 and 1952, plaintiff's income tax liability for 1951 was adjusted to $230,118.50 and his excess profit tax liability was adjusted to $51,630.77.

6. The allegations in paragraph numbered 6 are admitted, except it is alleged that the sum paid on June 13, 1952 was $79,184.83.

7. The allegations in paragraphs numbered 7, 8, 9, 10, and 11, are admitted.

12. The allegations in paragraph numbered 12 are admitted, except it is alleged that the sum paid on October 11, 1951 was $11,308.31.

13. The allegations in paragraphs numbered 13 and 14 are admitted.

15. The allegations in paragraph numbered 15 are de-

nied, except it is admitted that the aforesaid Revenue Agent's report, dated October 8, 1954, showed plaintiff liable for excess profits tax for 1951 in the amount of $51,630.77 and for 1952 in the amount of $8,151.10.

19. The allegations of paragraphs numbered 16, 17, 18, 19, 20 and 21 are admitted.

22. The allegations of paragraph numbered 22 are admitted, except it is alleged that the sum paid on June 14, 1955 was $173,195.75.

23. The allegations of paragraph numbered 23 are admitted, but it is not intended to admit any of the allegations contained in plaintiff's claims for refund not expressly admitted elsewhere in this answer.

24. The allegations of paragraph numbered 24 are admitted, but it is not intended to admit any of the allegations contained in plaintiff's claims for refund not expressly admitted elsewhere in this answer.

25. The allegations of paragraph numbered 25 are admitted.

26. The allegations of paragraph numbered 26 are denied.

27. The allegations of paragraph numbered 27 are admitted.

28. The allegations of paragraphs numbered 28, 29, 30, and 31 are denied, and it is alleged that the designated sections of the Internal Revenue Code of 1939 and 1954 speak for themselves.

32. Defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations of para-

graph numbered 32 of the complaint.

33. The allegations of paragraphs numbered 33 and 34 are denied.

35. Defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph numbered 35 of the complaint.

36. The allegations of paragraph numbered 36 are admitted, but it is not intended to admit any of the allegations contained in plaintiff's claims for refund not expressly admitted elsewhere in this answer.

37. The allegations of paragraph numbered 37 are admitted.

38. The allegations of paragraph numbered 38 are admitted, but it is not intended to admit any of the allegations contained in plaintiff's claims for refund not expressly admitted elsewhere in this answer.

39. The allegations of paragraph numbered 39 are admitted.

40. The allegations of paragraph numbered 40 are admitted, but it is not intended to admit any of the allegations contained in plaintiff's claims for refund not expressly admitted elsewhere in this answer.

41. The allegations of paragraphs numbered 41 and 42 are admitted.

43. The allegations of paragraph numbered 43 are admitted, but it is not intended to admit any of the allegations contained in plaintiff's claims for refund not expressly admitted elsewhere in this answer.

44. Defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph numbered 44 of the complaint.

45. The allegations of paragraphs numbered 45 through 54 are denied.

55. The allegations of paragraph numbered 55 are admitted.

WHEREFORE, defendant respectfully prays that judgment be entered in its favor with allowable cost.

WILLIAM C. CALHOUN
United States Attorney

CERTIFICATE OF SERVICE

I, WILLIAM C. CALHOUN, United States Attorney for the Southern District of Georgia, do herby certify that I have this date served the plaintiff, Merry Brothers Brick and Tile Company, with a copy of the foregoing answer, by this date mailing said copy to its attorneys of record, to-wit, FULCHER, FULCHER & HAGLER, at their last-known address, 410 Marion Building, Augusta, Georgia.

This 7th day of March, 1956.

WILLIAM C. CALHOUN
United States Attorney

U. S. District Court
Augusta Division
Filed in Office
March 2, 1956
Orlena T. Weaver
Deputy Clerk

UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF GEORGIA
AUGUSTA DIVISION

MERRY BROTHERS BRICK AND TILE COMPANY Plaintiff vs. UNITED STATES OF AMERICA Defendant	CIVIL ACTION NO. 752

MOTION TO AMEND COMPLAINT

Now comes the plaintiff, Merry Brothers Brick and Tile Company, in the above entitled cause, by its attorney, and moves the Court for leave to amend its complaint as follows:

1. By striking from paragraph 2 thereof the phrase, "and $504.33 of interest" with respect to the amount collected from plaintiff for the calendar year 1954.

2. By striking from paragraph 6 the following, "$78,184.83 on June 13, 1952", and inserting in lieu thereof the following: "$79,184.83 on June 13, 1952."

3. By striking paragraph 54 and inserting in lieu thereof the following:

"54. By reason of the facts set forth in this complaint, there is now due and owing from defendant to plaintiff the sum of $361,932.06, with interest thereon, as provided by law, from the dates of payment thereof. Of said sum, $140,624.37 was erroneously and illegally assessed against and collected from plaintiff as income tax, excess profits tax and interest thereon

for 1951, $82,749.53 was erroneously and illegally assessed against and collected from plaintiff as income tax, excess profits tax and interest thereon for 1952, $70,174.47 was erroneously and illegally assessed against and collected from plaintiff as income tax and interest thereon for 1953, and $68,383.69 was erroneously and illegally collected from plaintiff as income tax and interest thereon for 1954. The sum of $504.33 interest collected from plaintiff for the calendar year 1954, as shown in paragraph 22 hereof, was refunded to plaintiff on December 7, 1955."

4. By striking from paragraph 55 the figure "$362,436.39" and inserting in lieu thereof the figure "$361,932.06."

5. By striking from the prayer of said complaint the figure "$362,436.39" and inserting in lieu thereof the figure "$361,932.06".

Fulcher, Fulcher & Hagler
W. M. FULCHER
Counsel for Plaintiff.

410 Marion Building
Augusta, Georgia

UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF GEORGIA
AUGUSTA DIVISION

MERRY BROTHERS BRICK AND TILE COMPANY
Plaintiff
vs.
UNITED STATES OF AMERICA
Defendant

CIVIL ACTION NO. 752

The defendant consents to the amendendment of the complaint in said cause in the particulars set forth in the foregoing Motion for Leave to Amend.

This 5th day of April, 1956.

WILLIAM C. CALHOUN
United States Attorney

UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF GEORGIA
AUGUSTA DIVISION

MERRY BROTHERS BRICK AND TILE COMPANY
Plaintiff
vs.
UNITED STATES OF AMERICA
Defendant

CIVIL ACTION NO. 752

ORDER GRANTING MOTION TO AMEND COMPLAINT

Upon consideration of the motion of the plaintiff to amend its Bill of Complaint,

IT IS ORDERED by the Court that the said motion be and the same is hereby granted.

This 9 day of April, 1956.

F. M. SCARLETT
United States Judge

UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF GEORGIA
AUGUSTA DIVISION

MERRY BROTHERS BRICK AND TILE COMPANY, Plaintiff V. UNITED STATES OF AMERICA, Defendant	CIVIL ACTION NO. 732

STIPULATION

It is stipulated by and between the parties through their respective counsel, that the following facts and attached exhibits shall be taken as true, subject to the right of either party to introduce other facts and documents not inconsistent herewith, and subject to the right of either party to object to the relevancy or materiality of any of the facts or documents herein stipulated.

1. With regard to paragraph 12 of the Complaint and Answer, it is stipulated that the sum paid on or about October 11, 1954, was $11,580.34.

2. There is attached hereto as Exhibit "A" Department of Interior, Bureau of Mines, Form 6-1255A, being an example of the reports submitted to the Bureau of Mines by various clay miners and manufacturers of their production and use of clay. A report in this form is voluntarily submitted yearly by most of the clay producers in the United States.

3. There is attached hereto as Exhibit "B" a compilation of the nationwide use and sale of miscellaneous clay for 1951, 1952, and 1953 as prepared by the United States Bureau of Mines from the various reports submitted to it during said years. Line 1 of Exhibit "B" discloses that the following tons of clay were sold for use in the making of heavy clay products (heavy clay products being identified by the Bureau of Mines as building brick, paving brick, drain tile, sewer pipe and kindred products) during the years states:

1951	84,402	short tons
1952	230,295	short tons
1953	342,506	short tons

4. The examining revenue agent in arriving at the percentages set forth in paragraphs 37, 39, 41 and 42 of the Complaint, which allegations are admitted in the same paragraphs of the Answer, allowed as "mining processes" only those processes (a) through (e) as set forth in paragraph 35 of the Complaint. The set percentages were computed from taxpayer's cost accounting records.

This April 5, 1956.

Fulcher, Fulcher & Hagler
By: W. M. FULCHER
Attorneys for Plaintiff
WILLIAM C. CALHOUN
William C. Calhoun
United States Attorney
DAVID W. RICHTER
David W. Richter
Attorney, U. S. Dept. of Justice

U. S. District Court
Augusta Division
Filed in Office
April 11, 1956
Orlena T. Weaver
Deputy Clerk
(SEAL)

EXHIBIT A

Budget Bureau No. 42 R1221
Approval expires August 31, 1955.

The Defense Mobilization Agencies may receive a copy of your report subject to the approval of the Bureau of the Budget, in accordance with the Federal Reports Act of 1942. Persons who have access to individual company information are subject to penalties for unauthorized disclosure.

UNITED STATES
DEPARTMENT OF THE INTERIOR
BUREAU OF MINES
WASHINGTON 25, D. C.

FIRE CLAY, STONEWARE CLAY, AND MISCELLANEOUS CLAY OR SHALE IN 1954

Name And Location Of Mine Or Pit Covered By This Report:

Name

County State

Nearest City or Town

Please elaborate any change necessary for correct name and address.

Section I. INSTRUCTIONS

Please reply to all questions applicable to your operations and return this form as soon as possible in the enclosed envelope which requires no postage, or to the Ceramic and Fertilizer Materials Branch, United States Bureau of Mines, Washington 25, D. C.

A separate report is requested for each mine or pit. Additional forms will be furnished upon request. If separate reports are not feasible a combined report will be acceptable providing you furnish the names and locations of all mines and pits included in this consolidated report.

Be sure to insert name and location of mine or pit, if different from the mailing address to which this report is sent.

Estimates are acceptable wherever exact figures are not available.

If any figures are estimated, please follow figures with "est."

Section II. OWNERSHIP AND DESCRIPTION OF OPERATIONS.

(a) Type of operations covered by this report (check all appropriate boxes): Underground Mine ☐ Open-Pit Mine ☐

(b) If you acquired this mine or pit during the year, give name and address of former owner or operator and date on which you took possession.

(c) If you sold ☐ or leased ☐ (specify which) this mine during the year, give name and address of your successor and date on which you gave possession.

(d) If inactive during the entire year, please state whether shutdown was temporary ☐ or permanent ☐

Section III.—FLUAE FIRE CLAY, STONEWARE CLAY, AND MISCELLANEOUS CLAY OR SHALE SOLD OR USED OF YOUR OWN PRODUCTION.

For clay sold, report the value of sales f.o.b. mine shipping point. For clay of your own production used by you, estimate a market value f.o.b. mine or f.o.b. consuming plant. Do not report either for clay sold or for clay used by you such figures as the cost of production, royalty payments, percentage depletion allowances, or similar figures as equivalent to or in place of the actual or estimated market value. If you cannot estimate a market value for the clay used by you, leave the column blank.

The total tonnage reported in Columns (2) and (4), Section III must agree with the total tonnage reported in Columns (2) and (3), Section V.

If necessary, estimate tonnage and value of raw clay used.

Report quantities to the nearest ton.

Report value to the nearest dollar.

Kind of Clay	Clay of your own production sold, including stockpile withdrawals		Clay of your own production used, including stockpile withdrawals	
	Quantity Short tons	Market value of raw clay f.o.b. mine shipping point	Quantity Short tons	Market value of raw clay f.o.b. mine shipping point
(1)	(2)	(3)	(4)	(5)
Fire clay:				
(a) Plastic				
(b) Flint				
(c) Diaspore				
(d) Burley				
Stoneware clay				
Other (specify)				
Total fire clay and Stoneware clay				
Miscellaneous clay and shale				
Other (specify)				
Total Misc. clay				

Section IV.—PURCHASES

If you purchased clay, please list names and addresses of producers or suppliers. If space on form is not sufficient, attach additional sheet.

Proceed to the questions on the back of this schedule.

(OVER)

Section V.—USES: FIRE CLAY, STONEWARE CLAY, AND MISCELLANEOUS CLAY OR SHALE SOLD OR USED, OF YOUR OWN PRODUCTION

Please report in the following table raw clay of your own production, sold or used by you during the year, including clay withdrawn from stockpiles. Give actual figures if possible; otherwise please estimate. The total tonnage reported in Columns (2) and (3), Section V, must agree with the total tonnage reported in Columns (2) and (4), Section III.

If a detailed breakdown by uses is not available, please estimate, based on your best judgment.

Used for	Fire clay and stoneware clay Short tons (2)	Miscellaneous clay and shale Short tons (3)
Pottery and Stoneware:		
Stoneware		
Art pottery, flower pots, and glaze slip		
Refractories:		
Firebrick and block		
High alumina brick (Min. 50% Al_2O_3)		
Clay crucibles		
Glass refractories		
Zinc retorts and condensers		
Saggers, pins, stilts, and wads		
Mortar		
Foundaries, steelworks (bulk)		
Other refractories (specify)		
Heavy clay products:		
Building brick and tile, paving brick, drain tile, sewer pipe, etc.		
Architectural terra cotta		
Floor and wall tile		
Lightweight aggregate		
Portland and other hydraulic cements		
Filler:		
Rubber		
Linoleum and oilcloth		
Paint		
Insecticides and fungicides		
Fertilizer		
Plastics, organic		
Other filler uses (specify)		
Chemical (specify)		
Artificial abrasives		
Rotary-drilling mud		
Exports		
Other uses (specify)		
Total		

Section VI.—MISCELLANEOUS

(a) Please indicate briefly any factors affecting your mining operations during the year, such as labor conditions, price changes, etc., or new developments or trends in the clay industry or in consuming industries (technologic process, competing materials, or similar factors) influencing the demand for your product

(b) Give names and addresses of new clay producers in your vicinity.

(c) May the Bureau of Mines publish your production data?
(Non response will be interpreted as an affirmative answer.)

(Signature) (Official position)

MISCELLANEOUS CLAY—EXHIBIT "B"

Source	1951		1952		1953	
	S.T.	$	S.T.	$	S.T.	$
1. Sold for heavy clay products	84,402	104,555	230,295	252,895	342,506	554,614
2. Total sold (MY)	989,739	2,025,912	1,604,851	3,713,415	1,504,946	2,872,664
3. Sold for cement (MY)	658,450	660,936	790,531	813,301	734,706	783,725
4. Sold for other (2-1-3)	247,000	1,260,000	584,030	2,647,000	427,000	1,594,000
5. Total sold or used for heavy products (MY)	19,126,414		17,587,646		18,243,673	
6. Total sold or used (MY)	27,649,491	29,692,630	26,907,910	31,179,891	28,278,307	32,424,198

Miscellaneous Clay Sold for Heavy Clay Products, (As a Percent) of:

Source	1951	1952		1953	
		S.T.	%	S.T.	%
7. Total sold or used	(1÷6)	.30	.83	1.21	
8. Total sold or used for heavy products	(1÷5)	.44	1.31	1.88	
9. Total sold	(1÷2)	8.53	14.3	22.8	

Average Value of Miscellaneous Clay Product ($/S.T.)

Source	1951	1952		1953	
		S.T.	$	S.T.	$
10. Sold for heavy products (1)		1.24	1.10	1.62	
11. Total sold and used (6)		1.07	1.16	1.15	
12. Sold for cement (3)		1.00	1.03	1.06	
13. Used by producer for cement (MY)		1.02	1.00	.98	
14. Sold for other than heavy products and cement (4)		5.10	4.53	3.73	
15. Total sold (2)		2.05	2.31	1.91	
16. Total used by producer (MY)		1.04	1.10	1.10	

"MY" means published in Minerals Yearbook chapters.

Miscellaneous Clay Sold Which Was Used for Heavy Clay Products

	Source	1951		1952		1953	
		S.T.	$	S.T.	$	S.T.	$
17.	Ohio and New York	38,916	59,069	123,556	135,862	156,737	
				(No N.Y.)			
18.	Colorado	C	C	21,207	43,415	47,278	81,900
19.	California	O	O	C	C	6,639	5,417
20.	Indiana and Illinois	C	C	21,914	22,156	108,233	199,386
21.	Iowa Minnesota & Missouri	O	O	28,367	31,257	4,364	3,177
				(No Missouri)			
22.	New Jersey, Pennsylvania and North Carolina	C	C	C	C	18,782	16,972
23.	Other states which include Oklahoma, Montana Texas Colorado, Indiana, California, Pennsylvania, Washington, North Dakota & Wisconsin	45,486	45,486	35,251	20,205	3,273	11,315
24.	Total	84,402	104,555	230,295	252,895	342,506	554,614

"C" means combingd with "Other states" in order to avoid disclosure of individual firm's data.

S.T. Means Short Tons

MY Means Mineral Yearbook of the Bureau of Mines.

The data in row 1 and rows 17-24 were obtained from confidential questionnaires and tabulations sheets in the Ceramics and Fertilizer materials Branch files of the Bureau of Mines. The data cover those sales of miscellaneous clay which could be identified as used for heavy clay products and which were not considered to be transfers among different plants controlled by the one group. The data are not ordinarily published because they constitute such a small parts of the total that is is not considered worth the effort to edit and compile them seperately.

UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF GEORGIA
AUGUSTA DIVISION

MERRY BROTHERS BRICK AND TILE COMPANY, Plaintiff	
vs.	CIVIL ACTION NO. 752
UNITED STATES OF AMERICA, Defendant	

MOTION FOR SUMMARY JUDGMENT

Comes now the plaintiff, Merry Brothers Brick and Tile Company by its attorney, and moves the court for a summary judgment in its favor as provided by Rule 56 (a), Federal Rules of Civil Procedure, on the ground that there is no genuine issue as to any material fact, and that the plaintiff is entitled to a judgment as a matter of law.

In support of this motion, Affidavits of Kenneth H. Merry, Gilbert C. Robinson and Magdalen Gilbert are filed herewith.

Fulcher, Fulcher & Hagler
W. M. Fulcher
Counsel for Plaintiff

410 Marion Building
Augusta, Georgia

U. S. District Court
Augusta Division
Filed in Office
April 9, 1956
Deputy Clerk
Orlena T. Weaver

UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF GEORGIA

AUGUSTA DIVISION

MERRY BROTHERS BRICK AND TILE COMPANY Plaintiff vs. UNITED STATES OF AMERICA Defendant	CIVIL ACTION NO. 752

STATE OF GEORGIA
RICHMOND COUNTY

AFFIDAVIT OF KENNETH H. MERRY

Kenneth H. Merry, of the City of Augusta, County of Richmond, State of Georgia, having been first duly sworn deposes as follows:

1. I am the President and Treasurer of Merry Brothers Brick and Tile Company, the plaintiff in the above stated action, and which will be hereinafter referred to as the Company. The business now conducted by the Company was established in 1899 as a partnership between the late Arthur H. Merry and Ernest B. Merry. I came to work for the Company in 1919 and have worked in practically every department from mining to sales. I have held the office of President since 1943. I am a graduate Mechanical Engineer, having received my degree at the Georgia School of Technology. At present I am Vice President of the Southern Brick and Tile Manufacturers Association, to which office I was elected in May 1955. I have been active

in various capacities in such Association since it was organized about thirteen (13) years ago, and I have represented the Company on many occasions in the affairs of the Association during the absence of my brother, Guy H. Merry, a former Director, who is now deceased. Because of my position with the Company, and my experience in the brick and tile industry I have personal knowledge of the facts stated herein.

2. When I use the term "brick and tile clay" in this affidavit, I am referring to clay which is used to make common brick, drain and roofing tile, sewer pipe, flower pots, and kindred products.

3. The Company's Federal Income Tax Returns for the calendar years ending December 31, 1951, 1952 and 1953 were examined by an Internal Revenue Agent and a Revenue Agent's report dated October 8, 1954, stating the result of such examination was transmitted to the Company under date of June 6, 1955, by Paul Cobb, District Director of Internal Revenue in Atlanta.

4. Such Revenue Agent's report proposed deficiencies in the Company's income tax and excess profits tax for 1951 and 1952 and in the Company's income tax for 1953 on the basis of adjustments in the Company's net income and excess profits net income for 1951 and 1952, and in its net income for 1953, which adjustments included the disallowance of a portion of the depletion deduction which the Company had taken on its returns for each of those years. Attached hereto as Exhibit A is a true and correct copy of that portion of said Revenue Agent's report explaining the Revenue Agent's adjustment of the Company's deduction for depletion.

5. On May 21, 1955, the Company executed Treasury Department Form 870, waiving restrictions on the assessment

and collection of the proposed deficiencies, and on June 8, 1955, deficiencies for said years were assessed in accordance with said Revenue Agent's report.

6. On July 1, 1955, the Company paid such asserted deficiencies and interest thereon as follows:

Year	Tax Paid	Interest Paid
1951	$119,049.81	$21,574.56
1952	72,914.22	9,835.31
1953	65,351.15	4,823.32

7. The Company filed its Income Tax Return for the Calendar year 1954 and claimed a deduction for percentage depletion computed on the basis that the Commissioner had allowed the Company for 1951, 1952 and 1953, according to said Revenue Agent's report. Said return disclosed a tax liability of $278,139.05 of which $105,447.63 was paid March 15, 1955, and $172,691.42, together with interest of $504.33, was paid June 14, 1955.

8. On July 22, 1955, the Company filed with the Director of Internal Revenue in Atlanta, Georgia, claims for refund of income tax and excess profits tax and interest thereon for the calendar years 1951 and 1952, and for refund of income tax and interest for the calendar years 1953 and 1954. Copies of such claims are hereto attached as Exhibits B, C, D and E, respectively, and are made a part hereof.

9. On December 7, 1955, there was refunded to the Company the sum of $501.33, representing the interest paid by it on June 14, 1955, as shown in paragraph 7 hereof.

10. The Company owns and operates several clay pits

located in Richmond County, Georgia, near the City of Augusta. It is engaged in the business of mining clay from these pits and making brick and tile from such clay in two brick and tile plants, both of which are located near the clay pits.

11. The Company sells all of the clay which it mines in the form of burnt brick and tile, except for negligible amounts of raw clay, none of which is sold for use in the making of common brick and tile or kindred products. The relatively small sales of clay by the Company during 1951, 1952, 1953 and 1954 are shown in Exhibit F hereto attached as a part hereof. By Refergnce to said Exhibit it is seen that the ratio of the amount of clay sold in the raw state to the amount of clay processed and sold in the form of burnt brick and tile was .007233 for 1951, .005977 for 1952, .005467 for 1953, and .002967 for 1954. Of the clay sold in the raw state during those years, some was used for refractory materials, some was used as mud seals in well drilling operations, and some was sold for use in packing hooves of race horses and polo ponies, also for tennis courts and rose gardens. None of the raw clay sold by the Company was used in making brick and tile or kindred products.

12. I am familiar with the brick and tile industry in the United States. I have on many occasions visited various brick and tile plants in Georgia, and in other parts of the United States. I have observed the operations in the plants visited, their source of supply of clay and the marketing activities of those companies.

13. I know of no commercial market anywhere in the United States for brick and tile clay before it is made into burnt brick or tile. Usually, each producer of brick and tile

has its own clay pit or pits, and obtains its entire supply of brick and tile clay from such pit or pits. In the normal situation, a producer of brick and tile clay must process that clay into burnt brick and tile before obtaining a product which the producer can sell. It may be possible in unusual circumstances or a mine owner to sell negligible quantities of brick and tile clay before it is made into burnt brick and tile, and it may be that there actually are instances when such negligible quantities are sold, as stated in paragraph 11 hereof. However, such instances are rare and do not create an opportunity to sell more than a negligible quantity of clay, and do not create or establish a market for raw clay.

14. There is no market for the Company's brick and tile clay before it is made into burnt brick and tile. No one has ever offered to purchase any clay from the Company for the purpose of making brick or tile or kindred products, and the Company has never sold any clay for such purpose. No one has ever offered to sell brick and tile clay to the Company for its use in making brick or tile, and the Company has never bought any such clay for its use. The following are the processes applied by the Company to its raw clay in order to put it in the form of burnt brick and tile:

(a) The clay is mined at several different pits simultaneously by draglines and loaded in dump cars which operate on railroad tracks and carry the clay to the plant.

(b) The clay is dumped from the cars into large feeders which mix the clay and reduce the large chunks to a size that can be carried on a conveyor belt.

(c) The clay mined from the several different pits is discharged from the feeders on conveyor belts which carry it

first to a disintegrator or crusher and then to a storage shed, where it is blended and weathered.

(d) The clay blended and weathered in the storage shed is then loaded onto a conveyor belt which carries the clay to a set of smooth roll crushers, which further reduce the size of the chunks. In one of the plants there are two small additional granulators, or pug mills, through which the clay passes before reaching the smooth roll crushers.

(e) From these smooth roll crushers the clay is discharged onto another conveyor belt, which carries it by belt conveyors to another feeder where the clay is further blended or mixed.

(f) From the feeder the clay is discharged into the pug mill, which is a part of the brick machine wherein water is added as the final tempering process.

(g) From the pug mill the clay passes through a sealing die into and through a vacuum chamber where air is evacuated from the clay by a vacuum pump. The clay then falls into the extrusion section of the machine, where it is forced under pressure through various shapes of dies in long ribbons.

(h) The long ribbons of clay as extruded through the dies pass into the cutting machine, which cuts them into clay units of the desired size or length.

(i) The clay units as cut pass onto a conveyor belt and are then stacked by hand on dryer cars. These cars of brick are then moved to the dryer tunnels, where free water is evaporated from the clay units by warm air from fans which is blown on and over the units.

(j) When the free water is thus removed, the clay units are stacked either in periodic kilns, semi-continuous kilns, or continuous tunnel kilns.

(k) The clay units are then burned, either in periodic, semi-continuous or continuous tunnel kilns.

(l) The burnt brick and tile are then removed from the kilns.

(m) After they have been removed from the kilns, the burnt brick and tile are sorted and then loaded for shipment to purchasers.

15. The Company, for the calendar years 1951, 1952, 1953 and 1954, used the percentage depletion method in computing its depletion deduction for its clay pits.

(a) In its return for the calendar year 1951, it deducted $145,583.30 as depletion, which amount is equal to 5% of its net sales f.o.b. plant, loaded for shipment, of burnt brick and tile produced by the Company for that year, and is less than 50% of the net income from the sale of burnt brick and tile in such year.

(b) In its return for the calendar year 1952, the Company deducted $140,616.98 as depletion, which amount is equal to 5% of its net sales f.o.b. plant, loaded for shipment, of burnt brick and tile produced by the Company for that year, and is less than 50% of the net income from the sale of burnt brick and tile in such year.

(c) In its return for the calendar year 1953, the Company deducted $142,392.14 as depletion, which amount is equal to 5% of its net sales f.o.b. plant, loaded for shipment, of the burnt brick and tile produced by it for that year, and is less than 50% of the net income from the sale of burnt brick and tile in such year.

(d) In its return for the calendar year 1954, the Com-

pany deducted $18,803.91 as depletion. The computation of depletion for 1954 was on the basis and according to the method allowed by the Commissioner for the calendar years 1951, 1952 and 1953, pursuant to said Agent's report. The Company's net sales f.o.b. plant, loaded for shipment, of the burnt brick and tile produced by it for the calendar year 1954 is $3,000,220.53, and 5% of said amount is $150,311.00, which sum is less than 50% of the net income from the sale of burnt brick and tile in such year. By using the method of computation in said Agent's report, the Company's deduction for depletion represented 5% of $376,078.19 which amount is only 12.51 percent of the Company's net sales, f.o.b. plant, loaded for shipment, of burnt brick and tile produced by it in 1954.

16. The processes listed in paragraph 14 hereof are the ordinary treatment processes by which brick and tile clay generally is extracted from the ground and processed into brick and tile and are the processes normally used by the brick and tile industry in the United States.

KENNETH H. MERRY

Sworn to and subscribed before
me this 31st day of March, 1956.
MURIEL B. DAWSON
Notary Public
Richmond County, Georgia
My Commission expires:
June 4, 1956.

(SEAL)

EXHIBIT "A"

Name: Merry Brothers Brick and Tile Co.

SCHEDULE 1-A Year 1951

EXPLANATION OF ITEMS

(A) Depletion $126,934.08

A deduction for depletion was claimed on the return, computed on a basis of 5% of net sales. It is the position of the Government that percentage depletion should be computed on a basis of 5% of gross income from mining. There were no income figures from mining available. Therefore, a ratio of total mining costs to total cost of goods manufactured has been computed; and this ratio has been applied against the total net sales. The resulting figure represents gross income from mining on which the percentage depletion of 5% has been computed. See Exhibit K for details of computations.

SCHEDULE 4-A Year: 1952

EXPLANATION OF ITEMS

(A) Depletion $124,544.46

Same explanation as for adjustment items (a) Schedule 1-A See Exhibit K for details of computation.

SCHEDULE 7-A Year: 1953

EXPLANATION OF ITEMS

(A) Depletion $125,675.30

Same explanation as for adjustment item (a) on Schedule 1-A. See Exhibit K for details of computation.

EXHIBIT "K"

MERRY BROTHERS BRICK & TILE COMPANY

Computation of Percentage for Depletion

	1951	1952	1953
Total cost of goods manufactured	2,092,862.73	2,100,819.25	2,130,077.72
Cost of Mining: Clay Pit	141,791.73	130,821.89	121,908.62
Clay Storage	111,776.03	104,399.26	125,423.87
	256,517.76	240,221.15	250,332.49
Percent of mining costs to total costs	.1281	.1143	.1174
Gross sales per return	2,911,666.05	2,812,330.55	2,847,842.78
Gross Income from Mining:			
Gross sales multiplied by percent of mining costs to total costs	372,881.42	321,450.41	334,336.74
Percentage depletion allowable:			
5% of gross income from mining	18,639.22	16,072.52	16,716.84
Deduction claimed on return	145,583.30	145,616.78	142,392.14
Examine deduction	126,944.08	124,544.26	125,675.30

ANALYSIS OF CLAY SALES

Years 1951 thru 1954

EXHIBIT "F"

	Sales in Tons			
	1951	1952	1953	1954
Processed, and sold as Brick and Tile	399,403.41	379,539.13	405,024.15	425,609.01
Tons of Raw Clay	2,888.79	2,386.97	2,214.45	1,262.79
Ratio of Clay Sales to Brick and Tile Sales	.007233	.005977	.005467	.002967

UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF GEORGIA
AUGUSTA DIVISION

MERRY BROTHERS BRICK AND TILE COMPANY Plaintiff vs. UNITED STATES OF AMERICA Defendant	CIVIL ACTION NO. 752

STATE OF SOUTH CAROLINA
COUNTY OF PICKENS

Gilbert C. Robinson, of the city of Clemson, County of Pickens, State of South Carolina, having been first duly sworn, deposes and says:

1. I am a Ceramic Engineer, having received a Bachelor of Ceramic Engineering Degree at North Carolina State College. I am a registered professional engineer in the State of South Carolina, and Chairman of the Structural Clay Products Division of the American Ceramic Society. I am Professor of the Department of Ceramic Engineering at Clemson College, Clemson, South Carolina, where I have been for the past nine (9) years. I organized the Department of Ceramic Engineering at Clemson College six (6) years ago and have been head of that Department since then. After becoming a Professor at Clemson

College, and preparatory to organizing the Ceramic Engineering Department there, I visited the Ceramic Engineering Departments in all major colleges and universities throughout the United States having such department, and studied all phases of their operations and their relations to the ceramic industry. Prior to coming to Clemson, I did research work in the laboratory of the Tennessee Valley Authority at Muscle Shoals. I have published several pamphlets on raw materials in this area, which were given general distribution. I have written several articles, including the following: (1) "Limitations Placed on Speed of Firing by Raw Materials", which was published in the journal of the American Ceramic Society, (2) "South Carolina Raw Materials for Production of Light Colored Face Brick", (3) "Distribution and Properties of Shales of South Carolina", (4) "Structural Glazed Tile Industry for South Carolina", the last three articles named having been printed as bulletins of the South Carolina State Development Board. I have also made talks before conventions of the American Ceramic Society on quality control laboratories for structural clay products plants. Because of the positions I have held and my research work and experience in the field of ceramics, I have personal knowledge of the facts stated herein.

2. When I use the term "brick and tile clay" in this affidavit, I am refering to clay which is used to make common brick, drain and roofing tile, sewer pipe, flowerpots, and kindred products.

3. In connection with my work and research in the field of ceramics, I have had occasion to visit a number of brick and

tile plants of companies located in various parts of the United States. I have observed the operations in these plants, their source of supply of clay, and the marketing activities of these companies.

4. On a number of occasions I have visited the plants of Merry Brothers Brick and Tile Company, located at Augusta, Georgia, and have observed the clay pits from which that company obtains its clay. The clay used by Merry Brothers Brick and Tile Company is a surface clay of the type commonly used to make brick and tile in that area.

5. I am familiar with the processes used by Merry Brothers Brick and Tile Company in making brick and tile. Those processes are the ordinary ones by which brick and tile clay generally is extracted from the ground and processed into brick and tile, and are the processes normally employed in the brick and tile industry in the United States.

6. I know of no sales or the opportunity for the sale by Merry Brothers Brick and Tile Company of its clay, until the clay has been put into the form of burned brick and tile. I know of no sales of raw or partly processed brick and tile clay in the area surrounding Merry Brothers Brick and Tile Company clay pits. No market exists for Merry Brothers brick and tile clay until it has been treated to make burned brick and tile.

7. I am familiar with the marketability of brick and tile clay throughout the United States. Such clay is not commercially marketable until after it has been burned in a kiln so as to make the finished brick or tile or kindred products. There

may be some instances where there is opportunity to sell negligible quantities of such clays, but I know of no such instances. If there were any appreciable number of transactions in the United States involving the sale or purchase of such clay in a raw or partly processed state, at least some of these transactions would have come to my knowledge or attention. I know of no such purchases or sales. I know of no offers to purchase or sell such clay in any form other than burned brick or tile or kindred fired products.

8. I have never seen nor heard brick and tile clay referred to as an ore in any of the ceramic publications, or in the brick and tile industry. Brick and tile clay is not an ore, since it does not contain minerals that can be extracted profitably. When brick and tile clay is mined, all the material extracted from the ground is utilized.

GILBERT C. ROBINSON

Sworn to and subscribed before
me this 23rd day of March,
1950.

WILLIAM B. KELLER
Notary Public
My Commission Expires:
My commission expires at the
Pleasure of the Governor.

UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF GEORGIA
AUGUSTA DIVISION

MERRY BROTHERS BRICK AND TILE COMPANY,
Plaintiff,

vs.

UNITED STATES OF AMERICA,
Defendant.

CIVIL ACTION NO. 752

AFFIDAVIT OF MAGDALEN GILBERT

City of Washington
District of Columbia

ss.

Magdalen Gilbert, being first duly sworn according to law, deposes as follows:

1. I am now, and have been since 1940, Comptroller of the Structural Clay Products Institute (hereinafter sometimes referred to as "SCPI"). I have been employed by SCPI since its formation in November, 1934. By virtue of my position with SCPI, I have personal knowledge of the facts stated herein.

2. One of my duties as Comptroller of SCPI is to compile and keep current the mailing list of SCPI and the Directory of the structural clay products industry which SCPI publishes. The mailing list and the Directory include the name of every company of which we know which is in the business of making structural clay products, i.e., brick, structural tile and facing tile, whether or not such companies are members of SCPI. The Directory also shows the number of plants operated by each company. The mailing list and Directory do not include any

producers of drain tile or sewer pipe, unless such producers also make structural clay products or are members of SCPI. The mailing list and the Directory do not include companies in the business of making flower pots.

3. The mailing list and the Directory are constantly revised and kept up to date. All available sources, including personal contacts and newspaper and magazine articles, are checked for the names of any new companies or for any information as to the discontinuance of any company or of any plant. The mailing list and Directory are also reviewed annually by twenty-eight regional offices throughout the United States. If any company ceases to do business, we learn of it promptly by the return of mail sent to them.

4. The Directory of the structural clay products industry has been revised and republished in June, 1949, November, 1953, and April, 1955. I have just completed, in March, 1956, a new revision of this Directory. The mailing list and Directory show the following number of brick and tile companies and plants as of the following dates:

Date	No. of Companies	No. of Plants
June, 1949	641	756
November, 1953	579	723
April, 1955	563	710
March, 1956	566	708

5. The Bureau of the Census of the United States Department of Commerce compiles and publishes a Census of Manufacturers. The last such Census of Manufacturers was made in 1947, and the results of it were released in 1949. This census shows the number of establishments engaged in the production

of various clay products. A true and correct photostatic copy of the table giving this information is attached hereto as Exhibit A and is made a part hereof. This table shows the following number of establishments:

Brick and Hollow Tile	674
Sewer Pipe	69
Structural Clay Products, n.e.c.	161

The classification "Structural Clay Products, n.e.c." is explained in the table to consist of "establishments primarily engaged in manufacturing structural clay products, not elsewhere classified, such as architectural terra cotta, roofing tile, stove lining, flue lining, chimney pipes and tops, wall coping, segment blocks, drain tile, and quarry or promenade tile."

MAGDALEN GILBERT

Sworn and subscribed to before me this 28th day of March, 1956.

TERESA P. ZUICK
Notary Public
My Commission expires:
April 30, 1960
(SEAL)

Due and legal service of the foregoing Motion for Summary Judgment and of the supporting Affidavits is hereby acknowledged and further service waived.

This 5th day of April, 1956.

WILLIAM C. CALHOUN
United States Attorney

IN THE UNITED STATES DISTRICT COURT FOR THE
SOUTHERN DISTRICT OF GEORGIA
AUGUSTA DIVISION

MERRY BROTHERS BRICK AND TILE COMPANY, Plaintiff, v. UNITED STATES OF AMERICA, Defendant.	CIVIL ACTION NO. 752

DEFENDANT'S CROSS-MOTION FOR SUMMARY JUDGMENT

Defendant, through its attorney, William C. Calhoun, United States Attorney for the Southern District of Georgia, moves the Court to enter, pursuant to Rule 56 of the Federal Rules of Civil Procedure, a summary judgment in defendant's favor dismissing plaintiff's complaint on the ground that there is no issue as to any material fact and that defendant is entitled to judgment as a matter of law. This motion is based upon:

(a) The pleadings.

(b) The affidavits and briefs attached to plaintiff's motion for summary judgment.

(c) Stipulation of facts heretofore filed with this Court.

(d) The brief for the defendant attached hereto.

WILLIAM C. CALHOUN
United States Attorney

By: William T. Morton
Assistant U. S. Attorney

CERTIFICATE OF SERVICE:

This is to certify that I have on the 15th day of May, 1956, served a copy of the foregoing motion, with attachment, upon plaintiff herein by mailing same on same date to plaintiff's attorney of record, W. M. Fulcher, Esquire, in a franked envelope addressed to him at 410 Marion Building, Augusta, Georgia, deposited in the United States Mails.

WILLIAM T. MORTON
Assistant U. S. Attorney

U. S. District Court
Filed in Office
Augusta Division
May 15, 1956
Orlena T. Weaver
Deputy Clerk

UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF GEORGIA
AUGUSTA DIVISION

MERRY BROTHERS BRICK AND TILE COMPANY

vs.

UNITED STATES OF AMERICA

CIVIL ACTION NO. 752

This is an action for recovery of the principal amount of $361,932.06 paid by plaintiff as income and excess profits taxes, and interest thereon, for the calendar years 1951, 1952, 1953 and 1954. Deficiencies assessed in income and excess profits taxes for 1951 and 1952, and income taxes for 1953

which plaintiff claims should be refunded are as follows:

Year	Deficiency	Interest
1951	$121,017.18	$21,574.56
1952	84,458.15	9,835.31
1953	76,931.49	4,823.32

For 1954, plaintiff seeks to recover $68,383.69, which it claims it overpaid.

The only point at issue is the amount of percentage depletion properly allowable to plaintiff for each of the years mentioned.

Plaintiff moves the Court for summary judgment in its favor in accordance with the provisions of Rule 56(a) of the Federal Rules of Civil Procedure on the ground that the pleadings and affidavits attached to the motion show that there is no genuine issue as to any material fact and that plaintiff is entitled to a judgment as a matter of law.

Defendant moves the Court to enter a summary judgment in its favor, pursuant to Rule 56, dismissing the complaint on the ground that there is no issue as to any material fact and that defendant is entitled to judgment as a matter of law as shown by the pleadings, the affidavits attached to plaintiff's motion, and the stipulation of fact between the parties.

Plaintiff claims that under the applicable statutes, it is entitled to deduction for percentage depletion of its clay lands on the basis of five percent (5%) of the selling price, f.o.b. plant, le[illegible]d for shipment, of the burnt brick and tile which it produces, and relies upon UNITED STATES OF AMERICA vs. CHEROKEE BRICK AND TILE COMPANY, 5 Cir., 218

Federal 2d 128, which affirmed CHEROKEE BRICK AND TILE COMPANY v. UNITED STATES, 122 Federal Supp., 50.

Defendant contends, on the other hand, that to correctly compute depletion plaintiff's operations should be classified into two groups, with certain of its processes placed in a group termed "mining" and the remaining processes placed in a group termed "manufacturing". The Commissioner of Internal Revenue undertook to make such classification with respect to plaintiff's processes, which processes are hereinafter listed alphabetically, by placing in the so-called "mining" group those processes designated as (a) through (e), and placing in the so-called "manufacturing" group processes (f) through (m). The Commissioner determined that, in each year involved here, plaintiff's gross income from mining should be computed by dividing the direct mining costs by the total costs of mining and manufacturing, based upon his classification and terminology, and by then multiplying the resulting percentage by plaintiff's gross income. For the years in question, it was determined that plaintiff's gross income from mining amounted to the following percentages of its gross income from the sale of brick and tile, f.o.b. plant, loaded for shipment, to-wit:

Year	Percentage
1951	12.81
1952	11.43
1953	11.74
1954	12.51

Based upon the method of computation contended for by defendant, it is argued that the maximum depletion to which plaintiff is entitled is 5% of 12.81% of plaintiff's sales of brick and tile, f.o.b. plant, loaded for shipment for 1951, 5% of

11.43% of such sales for 1952, 5% of 14.74% of such sales for 1953, and 5% of 12.54% of such sales for 1954.

The plaintiff owns and operates several clay pits and is engaged in mining clay from these pits and making brick and tile therefrom in two plants located near the pits. The plaintiff sells all of the clay which it mines in the form of burnt brick and tile, except for negligible amounts of raw clay, none of which is sold for use in the making of brick and tile. In 1951 the ratio of sales of raw clay to the clay processed and sold as brick and tile was .007253; in 1952 such ratio was .005077; in 1953 the ratio was .005167; and in 1954 the ratio was .002967. Brick and tile clay on which a depletion allowance is granted is defined as including only clay which is used or sold for use in the making of common brick and kindred products. The raw clay sold by plaintiff does not come within this definition.

The processes by which plaintiff processes its raw clay into burnt brick and tile are as follows:

(a) The clay is mined at several different pits simultaneously by draglines and loaded in dump cars which operate on railroad tracks and carry the clay to the plant.

(b) The clay is dumped from the cars into large feeders which mix the clay and reduce the large chunks to a size that can be carried on a conveyor belt.

(c) The clay mined from the several different pits is discharged from the feeders on conveyor belts which carry it first to a di-integrator or crusher and then to a storage shed, where it is blended and weathered.

(d) The clay blended and weathered in the storage shed

is then loaded onto a conveyor belt which carries the clay to a set of smooth roll crushers, which further reduce the size of the chunks. In one of the plants there are two small additional granulators, or pug mills, through which the clay passes before reaching the smooth roll crushers.

(e) From these smooth roll crushers the clay is discharged onto another conveyor belt, which carries it by belt conveyors to another feeder where the clay is further blended or mixed.

(f) From the feeder the clay is discharged into the pug mill, which is a part of the brick machine wherein water is added as the final tempering process.

(g) From the pug mill the clay passes through a sealing die into and through a vacuum chamber where air is evacuated from the clay by a vacuum pump. The clay then falls into the extrusion section of the machine, where it is forced under pressure through various shapes of dies in long ribbons.

(h) The long ribbons of clay as extruded through the dies pass into the cutting machine, which cuts them into clay units of the desired size or length.

(i) The clay units as cut pass onto a conveyor belt and are then stacked by hand on dryer cars. These cars of brick are then moved to the dryer tunnels, where free water is evaporated from the clay units by warm air from fans which is blown on and over the units.

(j) When the free water is thus removed, the clay units are stacked either in periodic kilns, semi-continuous kilns, or continuous tunnel kilns.

(k) The clay units are then burned, either in periodic, semi-continuous or continuous tunnel kilns.

(l) The burnt brick and tile are then removed from the kilns.

(m) After they have been removed from the kilns, the burnt brick and tile are sorted and then loaded for shipment to purchasers.

It satisfactorily appears that these processes are the ordinary treatment processes by which brick and tile clay generally is extracted from the ground and processed into brick and tile, and that they are the processes normally employed by the brick and tile industry. The processes are not materially different from those of Cherokee Brick and Tile Company, but are basically and essentially the same processes. See CHEROKEE BRICK AND TILE COMPANY vs. UNITED STATES, Supra.

Section 114(b)(4)(A) of the Internal Revenue Code of 1939, provides that the allowance for depletion under Section 23(m) in the case of brick and tile clay shall be five percentum (5%) of the gross income from the property during the taxable year. Section 114(b)(4)(B) contains the following definition of gross income from the property, to-wit:

"As used in this paragraph the term "gross income from the property" means the gross income from mining. The term "mining" as used herein, shall be considered to include not merely the extraction of the ores or minerals from the ground, but also the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products . . ."

The same provision for depletion and the same definition of gross income from the property appear in Section 613(b)(5)

(A), Section 613(c)(4) and Section 613(c)(2) of the Internal Revenue Code of 1954.

It appears that in the Cherokee case the defendant similarly contended that only processes (a) through (c) should be considered mining, and that the depletion allowance should be limited to 5% of the income attributable to those processes to the exclusion of the remaining processes. In deciding the question adversely to defendant's contention, the Circuit Court of Appeals held that, because of the clear and unambiguous language of the statute, gross income from mining must include the income from ordinary treatment processes which must be applied to obtain the commercially marketable mineral product and that the statute makes no provision for excluding any processes before such a marketable product is reached. UNITED STATES vs. CHEROKEE BRICK AND TILE COMPANY, supra. See also T. L. TOWNSEND, ACTING DISTRICT DIRECTOR vs. THE HITCHCOCK CORPORATION, 4 Cir. 232 Fed (2) 111, affirming THE HITCHCOCK CORPORATION vs. T. L. TOWNSEND, ACTING DIRECTOR OF INTERNAL REVENUE, 132 F. Supp. 735, which follows the Cherokee case and places a similar interpretation upon the statute with respect to the mining and processing of talc.

The Cherokee decision is applicable and controlling here. Consequently, the contention that certain of plaintiff's processes used in producing brick and tile should be excluded and disregarded in determining income from mining is without merit and must be decided against defendant.

Defendant argues further that there exists a market for plaintiff's raw clay, and, consequently, the clay itself is plaintiff's first commercially marketable mineral product. In that connection, defendant refers to a report compiled from infor-

mation on questionnaires supplied by producers of clay to the Bureau of Mines, United States Interior Department, which report is a part of the stipulation between the parties. The report indicates that some clay was sold in the United States during 1951, 1952 and 1953 for use in the manufacture of heavy clay products, i.e., building brick and tile, paving brick, drain tile, sewer pipe and kindred products. It is contended that, as a result, market conditions do prevail for brick and tile clay.

The stipulated reports shows that of the total of 19,126,414 tons of clay sold or used for heavy clay products in 1951, 84,402 tons, or .44%, were sold; that of the total of 17,587,646 tons sold or used for such products in 1952, 230,295 tons, or 1.31%, were sold; and that of the total of 18,243,673 tons sold or used for those products in 1953, 342,506 tons, or 1.88%, were sold. Thus it appears that the quantity of clay sold each year is negligible in relation to the total.

In the Cherokee case it did not appear that there was a complete absence of sales of brick and tile clay throughout the country, as will be seen from that part of the agreement between the parties which states that "only negligible amounts of the brick and tile clay mined in the United States can be sold before being processed into burnt brick and tile." It is true that the figures showing the quantities which had been sold did not appear in the record there, as they do here, since in that case the parties agreed that such sales were negligible, while here the figures produced show them to be negligible. The Court does not consider that the Cherokee case can be distinguished on that account.

The amount of clay sold in this country for each year covered by the stipulated report was considerably less than the

clay mined by plaintiff alone, and the record shows that in 1953 there were 579 brick and tile companies in the United States operating 723 plants. This Court is of the opinion that only negligible amounts of the brick and tile clay mined in the United States can be sold before being processed into burnt brick and tile, and the Court so holds.

The explanatory statement which follows and refers to Exhibit B of the stipulation containing the data on sales is significant. It states

"The data in row 1 (clay sold for heavy clay products) and rows 17-21 (sales by States) were obtained from confidential questionnaires and tabulation sheets in the Ceramics and Fertilizer Materials Branch files of the Bureau of Mines. The data cover those sales of miscellaneous clay which could be identified as used for heavy clay products and which were not considered to be transfers among different plants controlled by the one group. The data are not ordinarily published because they constitute such a small part of the total that it is not considered worth the effort to edit and compile them separately."

On the basis of the undisputed facts it must be concluded that plaintiff's brick and tile clay is not commercially marketable until it is processed into burnt brick or kindred products.

It seems clear to the Court that the processes in which plaintiff is engaged are included in "mining", as the term is used and defined in the Internal Revenue Code. It follows that plaintiff's depletion allowance should be computed on the selling price of plaintiff's burnt brick and tile, f.o.b. plant, loaded for shipment, and that plaintiff is entitled to recover.

UNITED STATES vs. CHEROKEE BRICK AND TILE COMPANY, supra.

Judgment will be entered accordingly.

This 3rd day of July, 1956.

F. M. SCARLETT
United States Judge

U. S. District Court
Augusta Division
Filed in Office
July 5, 1956
Orlena T. Weaver
Deputy Clerk

UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF GEORGIA
AUGUSTA DIVISION

MERRY BROTHERS BRICK AND TILE COMPANY Plaintiff vs UNITED STATES OF AMERICA Defendant	CIVIL ACTION NO. 752

ORDER FOR SUMMARY JUDGMENT AND JUDGMENT

The above stated cause came on to be heard on motion of plaintiff for a summary judgment in its favor, pursuant to Rule 56(a) of the Federal Rules of Civil Procedure, and on the cross-motion of the defendant for a summary judgment in its favor dismissing the complaint, also pursuant to Rule 56, and the

Court having considered the pleadings in said cause, the affidavits of Kenneth H. Merry and Gilbert C. Robinson and Magdalen Gilbert in support of plaintiff's motion, together with the exhibits attached to such affidavits, and the stipulation between the parties, together with the exhibits attached thereto; having heard oral arguments; having found that there is no genuine issue as to any material fact and no controversial question of fact to be submitted to the trial court; and having concluded that the plaintiff is entitled to judgement as a matter of law.

IT IS HEREBY ORDERED, ADJUDGED AND DECREED that plaintiff's motion for a summary judgment in its favor be and the same is hereby granted and sustained and that defendant's motion for a summary judgment in its favor be and the same is overruled and denied.

IT IS FURTHER ORDERED, ADJUDGED AND DECREED that the plaintiff, Merry Brothers Brick and Tile Company, recover of the defendant, United States of America, the sum of Three Hundred Sixty-one Thousand Nine Hundred Thirty-two and 06/100 ($361,932.06) Dollars, consisting of Sixty-four Thousand Four Hundred Nineteen and 04/100 ($64,419.04) Dollars of income tax, Fifty-four Thousand Six Hundred Thirty and 77/100 ($54,630.77) Dollars of excess profits tax, and Twenty-one Thousand Five Hundred Seventy-four and 50/100 ($21,574.50) Dollars of interest paid by plaintiff for the calendar year 1951; Sixty-four Thousand Seven Hundred Sixty-three and 12/100 ($64,763.12) Dollars of income tax, Eight Thousand One Hundred Fifty-one and 10/100 ($8,151.10) Dollars of excess profits tax, and Nine Thousand Eight Hundred Thirty-five and 31/100 ($9,835.31) Dollars of interest paid by plaintiff for the calendar year 1952; Sixty-five Thousand Three Hundred Fifty-one and 15/100 ($65,-

351.15) Dollars of income tax and Four Thousand Eight Hundred Twenty-three and 32/100 ($4,823.32) Dollars of interest paid by paintiff for the calendar year 1953; and Sixty-eight Thousand Three Hundred Eighty-three and 69/100 ($68,383.69) Dollars of income tax paid by plaintiff for the calendar year 1954, with interest at the rate of Six Percent (6%) per annum as provided by law and the cost of this action for which plaintiff shall have execution in accordance with law.

Entered on Minute Book K at page 345.

ORLENA T. WEAVER
Deputy Clerk

This 3rd day of July, 1956.

F. M. SCARLETT
United States Judge

U. S. District Court
Augusta Division
Filed in Office
July 5, 1956
Curtis M. Ford,
Deputy Clerk

UNITED STATES DISTRICT COURT FOR THE
SOUTHERN DISTRICT OF GEORGIA
AUGUSTA DIVISION

MERRY BROTHERS BRICK AND TILE COMPANY Plaintiff vs UNITED STATES OF AMERICA Defendant	CIVIL ACTION NO. 752

DEFENDANT'S NOTICE OF APPEAL

Notice is hereby given that the United States of America, defendant in the above stated case, appeals to the United States Court of Appeals for the Fifth Circuit from the final judgment of the United States District Court, Southern District of Georgia, entered in this action on July 3, 1956.

WILLIAM C. CALHOUN
William C. Calhoun
United States Attorney

CERTIFICATE OF SERVICE

I, WILLIAM C. CALHOUN, United States Attorney for the Southern District of Georgia, do hereby certify that I have this date served the plaintiff, Merry Brothers Brick and Tile Company, with a copy of the foregoing notice of appeal, by this date mailing said copy to its attorneys of record, to-wit, FULCHER, FULCHER & HAGLER, ESQUIRES, at their last-known address, 110 Marion Building, Augusta, Georgia.

This 30th day of August, 1956.

WILLIAM C. CALHOUN
William C. Calhoun
United States Attorney

U. S. District Court
Augusta Division
Filed in Office
August 30, 1956
Curtis M. Ford
Deputy Clerk

UNITED STATES DISTRICT COURT FOR THE
SOUTHERN DISTRICT OF GEORGIA
AUGUSTA DIVISION

MERRY BROTHERS BRICK AND TILE COMPANY Plaintiff v. UNITED STATES OF AMERICA Defendant	CIVIL ACTION NO. 752

DEFENDANT'S DESIGNATION OF
RECORD ON APPEAL

Now comes William C. Calhoun, attorney for defendant in the above-stated case, and specifies the record to be sent up in said case to the United States Court of Appeals for the Fifth Circuit, in connection with defendant's appeal herein, as follows:

1. Defendant designates the entire record in this case, specifically including:
   (a) Plaintiff's original complaint;
   (b) Court's order enlarging time for filing defensive pleadings;
   (c) Answer of defendant, with certificate of service;
   (d) Plaintiff's motion to amend complaint and order allowing same;
   (e) Plaintiff's motion for summary judgment, with exhibits thereto;
   (f) Stipulation, filed April 11, 1956;
   (g) Defendant's cross-motion for summary judgment with defendant's brief and certificate of service attached;

(h) Opinion of the Court;

(i) Order for summary judgment and judgment dated July 3, 1956;

(j) Defendant's notice of appeal, with certificate of service;

(k) Order extending time for defendant to docket the record on appeal;

(l) Order directing that the Clerk transmit the original record in this case to the United States Court of Appeals for the Fifth Circuit; and

(m) This designation of record, with certificate of service.

This 29th day of October, 1956.

WILLIAM C. CALHOUN
United States Attorney

CERTIFICATE OF SERVICE

I, WILLIAM C. CALHOUN, hereby certify that a copy of the within and foregoing designation of record on appeal has been served upon the plaintiff herein by this date mailing such copy to their attorney of record, W. M. FULCHER, ESQUIRE, of Fulcher, Fulcher & Hagler, at his last-known address, to-wit, 410 Marion Building, Augusta, Georgia.

This 29th day of October, 1956.

WILLIAM C. CALHOUN

U. S. District Court
Augusta Division
Filed in Office
October 29, 1956
Curtis M. Ford
Deputy Clerk

IN THE DISTRICT COURT OF THE UNITED STATES FOR THE SOUTHERN DISTRICT OF GEORGIA.
AUGUSTA DIVISION

United States of America,
Southern District of Georgia, SS.

I, EUGENE F. EDWARDS, Clerk of the United States District Court for the Southern District of Georgia, do hereby certify that the above and foregoing 165 pages, numbered from 1 to 165 inclusive, is the complete original record in Civil Action No. 752, wherein The United States of America is the Appellant, and Merry Brothers Brick and Tile Company is the Appellee, as fully as the same remains of record in my said office at Augusta, in said Southern District of Georgia.

WITNESS my official signature and the seal of said Court affixed at Augusta in the Southern District of Georgia on this the 9th day of November, 1956, and in the 181st year of the Independence of The United States of America.

EUGENE F. EDWARDS, CLERK.
Orlena T. Weaver
By (Orlena T. Weaver)
Deputy Clerk.

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

UNITED STATES OF AMERICA, Appellant, v. MERRY BROTHERS BRICK AND TILE COMPANY, Appellee.	No. 16,373.

STATEMENT OF POINTS TO BE RELIED ON UPON APPEAL BY APPELLANT—FILED NOVEMBER 8, 1956

Comes now the United States of America, Appellant in the above-styled case and lists the following points to be relied on upon appeal:

1. That the Court below erred in holding that under Section 114(b) (4), (B) of the Internal Revenue Code of 1939, and Section 613(c) of the Internal Revenue Code of 1954, "gross income from the property" includes all of the income from the extraction of the clay from the ground and from the processes which a miner of such clay must normally apply to the clay in order to convert it into a product for which there exists a commercial market.

2. That the Court below erred in its holding that all of the processes applied by plaintiff to its clay in order to obtain finished burnt tile and brick are, within the meaning of Section 114(b) (4) (B) of the Internal Revenue Code of 1939, and Section 613(c) of the Internal Revenue Code of 1954, the ordinary treatment processes normally applied by miners or operators in order to obtain the commercially marketable "mineral product or products."

3. That the Court below erred in holding that Treasury Regulations 118, Section 39.23(n)-1, are invalid where they exclude any of the processes applied by plaintiff to its clay to obtain finished burnt tile and brick from the statutory term "ordinary treatment processes."

WILLIAM C. CALHOUN
William C. Calhoun
United States Attorney

Appellant's Designation as to Printing Record—Filed November 8, 1956.

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

UNITED STATES OF AMERICA,

Appellant,

v.

MERRY BROTHERS BRICK AND TILE COMPANY,

Appellee.

(Designation of Record to be Printed In Appeal.)

No

The Appellant, United States of America, through its attorney, William C. Calhoun, United States Attorney for the Southern District of Georgia, and pursuant to Rule 23 of the Fifth Circuit Court of Appeals Rules, hereby designates the parts of the record to be printed on appeal to the United States Circuit Court of Appeals for the Fifth Circuit, as follows:

1. The complaint.
2. The answer to complaint.
3. Motion to amend complaint.
4. Order of Court granting motion to amend complaint.
5. Stipulation, excluding Exhibits A and B attached thereto.
6. Plaintiff's motion for summary judgment, including the affidavits and exhibits attached to the affidavits, as follows:
   (a) Affidavit of Kenneth H. Merry, including Exhibits A and F, but excluding Exhibits B, C, D, and E attached thereto.
   (b) Affidavit of Gilbert C. Robinson.

(c) Affidavit of Magdalen Gilbert, excluding Exhibit A attached thereto.

7. Defendant's cross-motion for summary judgment.

8. Memorandum opinion of the Court.

9. Order for summary judgment and judgment of the Court.

10. Notice of appeal.

11. Designation of record on appeal.

12. Statement of points to be relied on upon appeal by Appellant.

13. Clerk's certificate.

/s/ William C. Calhoun
WILLIAM C. CALHOUN
United States Attorney

CERTIFICATE OF SERVICE

I, William C. Calhoun, United States Attorney for the Southern District of Georgia, do hereby certify that I have this date served the Appellee, Merry Brothers Brick and Tile Company, with a copy of the foregoing designation of record to be printed on appeal, by this date mailing said copy to its attorneys of record, to-wit, Fulcher, Fulcher & Hagler, Esquires, at their last-known address, 410 Marion Building, Augusta, Georgia.

Done this 6th day of November, 1956.

/s/ William C. Calhoun
WILLIAM C. CALHOUN
United States Attorney

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

UNITED STATES OF AMERICA,

Appellant

vs. NO.

MERRY BROTHERS BRICK AND TILE COMPANY

Appellee

SUPPLEMENTAL DESIGNATION OF RECORD TO BE PRINTED ON APPEAL

The Appellant, United States of America, through its attorney, William C. Calhoun, United States Attorney for the Southern District of Georgia, and the Appellee: Merry Brothers Brick and Tile Company, through its attorney, W. M. Fulcher, pursuant to Rule 23 of the Fifth Circuit Court of Appeals Rules, do, by agreement, hereby file this their joint supplemental designation of certain parts of the record to be printed on appeal to the United States Circuit Court of Appeals for the Fifth Circuit, in addition to the parts of the record heretofore designated by the Appellant, as follows:

1. Exhibit A attached to the Stipulation.
2. Exhibit B and the explanatory suffix annexed thereto attached to the Stipulation.
3. Supplemental designation of record to be printed on appeal.

WILLIAM C. CALHOUN
United States Attorney

W. M. FULCHER
Attorneys for Appellee

APPE

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JOHN T. FEY, Clerk

TRANSCRIPT OF RECORD

IN THE

UNITED STATES COURT OF APPEALS

FIFTH CIRCUIT

No. 16323

ITED STATES OF AMERICA,

Appellant,

versus

LIANCE CLAY PRODUCTS COMPANY,

Appellee.

PEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF TEXAS

(Original Record Received October 8, 1956)

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FEEHAN, Jr.
CLERK

U. S. COURT OF APPEALS
FILED
OCT 8 1956
JOHN A. FEEHAN, JR.
Clerk

COMMERCIAL RECORDER, FORT WORTH, TEXAS—12-6-56—50

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TRANSCRIPT OF RECORD

IN THE

UNITED STATES COURT OF APPEALS

FIFTH CIRCUIT

No. 16323

UNITED STATES OF AMERICA,

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versus

RELIANCE CLAY PRODUCTS COMPANY

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(Original Record Received October 8, 1956).

U. S. COURT OF APPEALS
FILED
OCT 8 1956

JOHN A. FEEHAN, JR.
Clerk

STIPULATION AS TO PRINTING RECORD

Filed 11 10 56

NO. 16,323

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

UNITED STATES OF AMERICA,

Appellant

versus

RELIANCE CLAY PRODUCTS COMPANY,

Appellee

STIPULATION AS TO PRINTING OF RECORD

It is hereby stipulated by and between the parties hereto that it is not necessary to print plaintiff's Exhibit No. 2, being Stipulation No. 2, in its entirety

and it is agreed that the only portions of plaintiff's Exhibit No. 2 that are to be printed are Pages 1, 2, 3, 4, 5, 6 and 16 of Part I; Pages 19, 32 and 33 of Part II; and all of the pages of Part III, being Pages 39, 40 and 41.

Dated at Dallas, Texas, this the 8 day of November, 1956.

/s/ Heard L. Floore
Heard L. Floore,
United States Attorney

/s/ John C. Ford
John C. Ford, Assistant
United States Attorney

Attorneys for Defendant-Appellant,
United States of America

/s/ George S. Terry
George S. Terry,
Attorney for Plaintiff-Appellee,
Reliance Clay Products Company

CAPTION

BE IT REMEMBERED, that at a regular term of the United States District Court in and for the Northern District of Texas, begun and holden at Dallas, Texas, on the 15th day of May, A.D. 1956 and which said term adjourned on the 6th day of August, A.D. 1956, the Honorable William H. Atwell, United States District Judge for the Northern District of Texas, presiding, the following proceedings were had and the following cause came on for trial and was tried, to-wit:

No. 6400-Civil

Reliance Clay Products Company

versus

United States of America.

COMPLAINT

Filed Feb. 8, 1956

1.

Plaintiff brings this action against defendant pursuant to Section 1346(a)(1) of Title 28 of the United States Code, Act of June 25, 1948, c. 646, 62 Stat. 869, 933, as amended by the Act of May 24, 1949, c. 139, Par. 80(a), 63 Stat. 89, 101, as amended by the Act of July 30, 1954, c. 648, 1, 68 Stat. 589.

2.

This action is brought for the recovery of:

(a) $22,944.20 of income tax and interest thereon from the date of payment for the calendar year 1951; and

(b) $3,228.61 of income tax and interest thereon from the date of payment for the calendar year 1952.

3.

Plaintiff is a corporation incorporated and doing business under the laws of the State of Texas with its principal place of business at Dallas, Dallas County, Texas, within this District and division.

4.

Plaintiff keeps its books and reports for Federal Income Tax returns, on the accrual basis method of accounting, on a calendar year basis.

5.

Within the time prescribed by law, plaintiff made and filed its income tax returns for the calendar years 1951 and 1952, showing an income tax liability of $37,389.60 for 1951 and $4,735.55 for 1952, and no excess profits tax liability for either year.

6.

The income tax liabilities shown on such returns were paid on the following dates:

(a) Calendar year 1951 Return:

13,086.36 on March 1, 1952
24,303.24 on June 8, 1952

37,389.60

(b) Calendar year 1952 Return:

1,895.55 on March 14, 1953
1,420.00 on June 13, 1953

1,420.00 on August 11, 1953

4,735.55

Checks in payment were presented on or before the due dates required by law.

7.

The Commissioner of Internal Revenue, hereinafter sometimes referred to as the Commissioner, caused the aforesaid income tax returns of plaintiff for 1951 and 1952 to be examined and Revenue Agent's Reports to be submitted as follows:

(a) For 1951, the Revenue Agents' Report dated February 2, 1953, stating the result of such examination was transmitted to plaintiff under date of February 18, 1953, by Ellis Campbell, Jr., District Director of Internal Revenue in Dallas, Texas. Such report allowed plaintiff a deduction for percentage depletion computed as stated in paragraph 21, *infra*.

(b) For 1952, the Revenue Agents' Report dated October 28, 1954 stating the result of such examination, was transmitted to plaintiff under date of December 7, 1954, by Ellis Campbell, Jr. District Director of Internal Revenue in Dallas, Texas. Such report allowed plaintiff a deduction for percentage depletion computed as stated in paragraph 21, *infra*.

8.

The Revenue Agents' Reports referred to in paragraph 7, *supra*, proposed deficiencies in income taxes as follows:

(a) For 1951, of $46,994.96 on the basis that the deduction for percentage depletion and the deduction for depreciation which plaintiff had taken on its return was excessive.

(b) For 1952, of $3,228.61 on the basis that the deduction for percentage depletion which plaintiff had taken on its return was excessive.

9.

(a) Pursuant to such Revenue Agents' Report for 1951, the Commissioner made an additional assessment of $9,652.89 of income tax and of $562.64 of interest thereon representing additional amounts due on the depreciation adjustment referred to in paragraph 8, *supra*, which $10,215.53 was received by the Commissioner on March 20, 1953 (account #529000). Subsequent thereto, and pursuant to such Revenue Agents' Report, the Commissioner made an additional assessment of $37,341.47 of income and excess profits taxes (representing $28,722.00 of income taxes and $8,619.47 of excess profits taxes) and of $5,233.94 of interest thereon, which was received by the Commissioner on August 6, 1954 (account #528906).

(b) Of the original refund claim of $37,341.47, $8,619.47 was refunded by the Government, this being the excess profits tax paid which it was determined was erroneously calculated and it was agreed by the taxpayer that $5,777.80 should be eliminated since this item was based on transportation costs not subject to depletion, leaving the total amount of disallowed depletion claimed in this suit of $22,944.20, together with interest as provided by law.

(c) Pursuant to such Revenue Agent's Report for 1952, the Commissioner made an additional assessment of $3,228.61 of income tax and of $329.76 of interest thereon representing additional amounts due on the depletion adjustment referred to in paragraph 8, *supra*, which total of $3,558.27 was collected by the Commissioner through a credit against an overassessment of $8,619.47 representing excess profits taxes refunded as a result of the Revenue Agents' Examination for 1952 referred to in paragraph 7, *supra*. (Reference Schedule No. IT:B-1849, with no date.)

10.

On July 27, 1955, plaintiff duly filed with the District Director of Internal Revenue for the Second District of Texas at Dallas, Texas, a claim for refund of income taxes for 1951, and also a claim for refund of income taxes for 1952. These two separate claims represented the additional amounts paid for the adjustments to depletion pursuant to such additional assessments referred to in paragraph 9, *supra*.

Such claims for refund alleged that under Section 114 of the Internal Revenue Code of 1939, plaintiff is entitled to a percentage depletion deduction on its deposits of brick and tile clay, computed on the selling price, f.o.b. plant, loaded for shipment, of the burnt brick and tile which it produces. Such deductions are greater than those allowed by the Revenue Agents' Reports referred to in paragraph 7, *supra*. Such claims for refund set forth the grounds and reasons upon which this suit is brought. True and correct photostatic copies of the claims for refund for 1951 and 1952 respectively are attached to this petition and marked as Exhibits A and B and are made a part hereof for all purposes as though set out in full herein.

11.

On January 13, 1946 Ellis Campbell, Jr. the District Director of Internal Revenue, Dallas, Texas under Section 3772(a)(2) of the Internal Revenue Code of 1939 (Sec. 6532(a)(1) of the Code of 1954) mailed by registered mail separate notices of disallowance of the 1951 and 1952 claims for refund of income taxes filed on July 27, 1955. True and correct copies of such notices of disallowance are attached hereto and marked Exhibits C and D and made a part hereof for all purposes as though copied in full herein. The claims for refund were disallowed on the ground that the amounts of the deductions for percentage depletion which plaintiff was claiming was excessive and that plaintiff therefore had not overpaid its taxes.

12.

If plaintiff is entitled to a deduction for depletion as alleged in paragraph 21, *infra*, plaintiff has overpaid its income taxes in the amount of $22,944.20 for 1951 and in the amount of $3,228.61 for 1952.

13.

Plaintiff owns and operates two clay pits, one located in Smith County, Texas, near Lindale, Texas, and one located in Palo Pinto County, Texas, near Mineral Wells, Texas. It is engaged in the business of mining clay from these pits and making brick and tile from such clay in two brick and tile plants located near the pits.

14.

Section 23(m) of the Internal Revenue Code of 1939 provides for a deduction in computing net income of an allowance for depletion of "mines, oil and gas wells, other natural deposits, and timber." Section 114(b)(4)(A) of the Internal Revenue Code, effective on and after January 1, 1951, provides that the allowance for depletion under Section 23(m) in the case of "brick and tile clay" shall be 5% of the "gross income from the property" during the taxable year, but not to exceed 50% of taxpayer's net income from the property, computed without allowance for depletion.

15.

The term "gross income from the property" as used in Section 114(b)(4)(A) is defined in Section 114(b)(4)(B) which states that "gross income from the property" means the gross income from mining, and that "'mining' as used herein shall be considered to include not merely the extraction of the ores or minerals from the ground but also the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products . . ."

16.

There is no clay which by its physical or chemical characteristics can be identified as being only brick and tile clay. The term "brick and tile clay" as used in Section 114(b)(4)(A) of the Code means clay which is in fact used or for use in the production of brick and tile and kindred products, and does not include clay used for any other purpose.

17.

The treasury allows the deduction for depletion of "brick and tile clay" on a percentage basis only for clay used or for use in the production of common brick and tile and kindred products. Section 29.23(m)-5 of Treasury Regulations 111, as amended by T.D. 6031, approved July 14, 1953, defines "Clay, brick and tile", as follows:

"Clay used or sold for use in the manufacture of common brick, drain and roofing tile, sewer pipe, flower pots and kindred products (other than clay specifically identified as a clay for which a 15 percent rate of percentage allowance is provided)."

18.

Plaintiff sells all of the clay which it mines in the form of burnt brick and tile.

19.

(a) As such clay is defined in paragraphs 16 and 17, *supra*, there is no market for the brick and tile clay mined by plaintiff before it is put in the form of burnt brick and tile.

(b) Of the brick and tile clay mined in the United States, there is opportunity for the sale of only a negligible quantity before it is put in the form of burnt brick and tile.

20.

The following are the processes applied by plaintiff to the raw clay in order to put it in the form of "saleable ware", in burnt brick or tile:

(a) The clay is mined by a drag line and loaded in dump trucks which carry the clay to a nearby plant.

(b) The clay taken to the plant is sometimes weathered in a storage shed.

(c) The clay is either dumped directly from the dump truck or is taken from the storage shed and placed in a feeder from which the clay passes into a dry pan crusher, which crushes and grinds the clay.

(d) The clay is discharged from the dry pan crusher onto the elevator belt which carries it to a screen.

(e) The clay passes through the screen into a bin; from the bin the clay passes into a feeder.

(f) The clay is discharged from the feeder into the pug mill, which is a machine wherein water is added as the final tempering process.

(g) From the pug mill the clay passes into the brick or tile machine. It first goes into an evacuation chamber where air is evacuated from the clay by a vacuum pump. The clay then passes into the extrusion section of the machine where it is forced under pressure through various types of dies in long ribbons.

(h) The long ribbons of clay as extruded through the dies pass into the cutting machine which cuts them into clay units of desired size.

(i) The clay units as cut pass onto a conveyor belt and are then stacked onto dryer or kiln cars which are moved to the dryer tunnels or to the continuous tunnel-kiln, where free water is evaporated from the clay units by open gas fires, or waste heat from kiln.

(j) When the free water is thus removed the clay units are either stacked in periodic kilns, or in the case of continuous or tunnel-kilns, are left on the kiln cars which continue from the dryer to the kiln.

(k) The clay units are then burned by natural gas fires whether in periodic or continuous (tunnel) kilns.

(l) The burnt brick and tile is then removed from the kilns.

(m) After it has been removed from the kilns the burnt brick and tile is either stacked on the yard or loaded directly for shipment to purchasers.

21

In 1951, plaintiffs receipts from the sale of brick and tile which it produced were $1,228,484.96. Transportation costs of $227,696.49 are included in the selling price. This results in a selling price of $1,000,788.47 subject to depletion. Five percent (5%) of such amount is $50,039.42 and is less than 50% of the net income from such sales.

In 1952, plaintiffs receipts from the sale of brick and tile which it produced were $1,102 338.18. Transportation costs of $251,306.91 are included in the selling price. This results in a selling price of $851,031.27 subject to depletion. Five percent (5%) of such amount is $42,551.56, and is more than 50% of the net income of $31,570.34 on such sales. The limitation on the deduction for depletion of fifty percent (50%) of the net profits results in an allowable deduction for depletion of $15,785.17.

22.

The deductions which the Commissioner allowed plaintiff for percentage depletion in accordance with the Revenue Agents' Reports referred to in paragraph 7, *supra*, were as follows:

(a) For 1951, the Revenue Agent arrived at a cost figure which was arbitrarily termed "mining". All other costs of the plaintiffs income tax return were classified in three ways: (1) Manufacturing, (2) selling, and (3) administrative.

The Agents' Report assumed there would be profits earned on the (1) Mining costs, (2) manufacturing costs and (3) selling costs, but no profits on the (4) administrative costs. The administrative costs were then allocated to the other three classifications in accordance with the percentage of costs of each, without the administrative costs, as follows:

	Direct Total Amount		Administrative	Total
Mining	78,842.90	7.70	4,186.43	83,029.33
Manufacturing	612,802.89	59.83	32,529.08	645,331.97
Selling	332,557.55	32.47	17,653.67	350,211.22
	1,024,203.34	100.00	54,369.18	1,078,572.52

To the manufacturing expenses was then added the opening inventory of $21,383.36 and the year end closing inventory of $43,860.74 was deducted. Based on total costs, the Revenue Agents' Report assumed that each operation of mining, manufacturing and selling would earn a share of the eventual profit of the company as follows:

	Adjusted Total Cost Amount		Profits Allocated	Total
Mining	83,029.33	7.86	13,554.06	96,583.39
Manufacturing	622,854.59	58.98	101,707.22	724,561.81
Selling	350,211.32	33.16	57,182.28	407,393.50
	1,056,095.24	100.00	172,443.56	1,228,538.70
Difference not located by Revenue Agent				53.74
Total Sales				1,228,484.96

As a result of assuming the plaintiff had a commercially marketable product at the end of the "mining" stage and adding to such costs of mining an assumed profit on this raw material, the Revenue Agents' Re-

port allowed a five percent (5%) depletion only on the assumed selling price of $96,583.39, or a total depletion of $4,829.17.

(b) For 1952, the Revenue Agent arrived at a cost figure which was termed "mining". All other costs of the plaintiffs income tax return were classified as: (1) manufacturing expense, (2) handling expense, (3) selling expense, (4) other expense, and (5) administrative expense.

After allocation of the Administrative expenses and adjustment for opening and closing inventories as outlined in paragraph 22(a), *supra*, the Revenue Agents' Report assumed that each operation would result in a share of the eventual profit of the company as follows:

	Adjusted Total Cost Amount	%	Profits Allocated	Total
Mining	110,302.93	10.30	3,251.75	113,554.68
Manufacturing	427,221.86	39.89	12,596.57	439,818.43
Handling	147,095.96	13.74	4,337.76	151,433.72
Selling	383,340.11	35.80	11,302.18	394,642.29
Other	2,806.98	.26	82.08	2,889.06
	1,070,767.84	100.00	31,570.34	
Gross Sales				1,102,338.18

As a result of assuming the plaintiff had a commercially marketable product at the end of the "min-

ing" stage and adding to such costs of mining an assumed profit on this raw material, the Revenue Agents' Report allowed a five percent (5%) depletion of $5,677.73 on the assumed selling price of $113,554.68.

23.

(a) The processes listed in paragraph 20, *supra*, are the ordinary ones by which brick and tile clay generally is extracted from the ground and processed into brick and tile.

(b) In the case of brick and tile clay, burnt brick and tile are "the commercially marketable mineral product or products" as that term is used in Section 114 (b)(4)(B) of the Internal Revenue Code of 1939, as amended, and the processes described in paragraph 20, *supra*, are within the meaning of that section, "the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products"

24.

Plaintiff was entitled to a minimum depletion deduction of $50,039.42 for the year 1951 and of $15,785.17 for the year 1952. All the income attributable to extracting the clay from the ground and to the processes applied to produce the burnt brick and tile and load it for shipment is properly income from "mining" and thus "gross income from the property"; as those

terms are defined in Section 114(b)(4)(B) of the Internal Revenue Code of 1939, as amended.

25.

The action of the Commissioner, described in paragraph 22, *supra*, in excluding from "mining" a part of the ordinary treatment processes applied by the plaintiff to produce burnt brick and tile, thus excluding from "gross income from the property" the income attributable to such processes, and in limiting plaintiff's deduction for depletion to $4 829.17 for 1951 and to $5,677.73 for 1952 was erroneous, illegal, and without warrant in law.

26.

By reason of the facts set forth in this complaint, there is now due and owing from defendant to plaintiff the sum of $22,944.20 for 1951, and $3,228.61 for 1952 with interest thereon as provided by law from the dates of payment thereof. Such sums of $22,944.20 and $3,228.61 were erroneously and illegally collected from plaintiff as income taxes for the calendar years 1951 and 1952.

Although payment thereof has been demanded, no part of the sums of $22,944.20 and $3,228.61 have been credited, remitted, refunded or repaid to the plaintiff or to anyone on its account.

WHEREFORE, plaintiff demands judgment against defendant in the principal sums of $22,944.20 and $3,228.61 and interest thereon as provided by law, together with costs.

Respectfully submitted,

CHAS. D. TURNER
GEORGE S. TERRY
BY s George S. Terry, Jrg

Attorneys for Plaintiff,
Reliance Clay Products Company

OF COUNSEL:

TURNER, RODGERS, WINN, SCURLOCK & TERRY
2400 Republic National Bank Building
Phone: RIverside 9551
Dallas, Texas

EXHIBIT A

Form 843

TREASURY DEPARTMENT
Internal Revenue Service
(Revised Jan. 1946)

CLAIM

To Be Filed With The Collector Where Assessment Was Made or Tax Paid

Received Jul 27 1955 Dist. Director Int. Rev., Dallas

State of Texas
County of Dallas

Name of taxpayer or purchaser of stamps Reliance Clay Products Co. (A Corporation)

Business address P. O. Box 13226, Dallas, Texas

Residence 2220 Shorecrest Drive

1. District in which return (if any) was filed 2nd Dallas, Texas

2. Period (if for income tax, make separate form for each taxable year) from 1/1/51 19 , to 12/31/51 19

3. Character of assessment or tax Income and Excess Profits

6. Amount to be refunded as is legally refundable, plus interest, including $ 37,341.47

8. The time within which this claim may be legally filed expires, under section 3226 of Code on August 10, 1956.

Per exhibits attached which are incorporated as a part of this claim as though fully set-out on this form.

Signed Reliance Clay Products Co.

By /s/ George H. Harmon
President

Sworn to and subscribed before me this
11th day of July, 1955

/s/ James E. Strum
Notary Public, Dallas County, Texas

RELIANCE CLAY PRODUCTS CO.
FORM 843, REFUND CLAIM
12-31-51

Net Income Per RAR, dated February 2, 1953, H. A. Potwin		160,127.08
Plus Depletion allowed by RAR		4,829.17
		164,956.25
Less: Depletion computed as follows:		
Gross Sales - RAR	1,228,484.96	
Depletion Allowance 5%		61,424.25
		103,532.00

INCOME TAX COMPUTATION

Net Taxable Income	103,532.00	
Taxable at 50 3/4% less $5,500.00		47,042.49
Assessed Per RAR, and Paid		84,383.96
		37,341.47

BASIS FOR CLAIM OF REFUND FOR TAX ILLEGALLY COLLECTED

A. The Reliance Clay Products Company, taxpayer and petitioner here, was entitled under the provisions of Title 26, Section 114, Subsection B(4ab), U. S. Code, to a deduction for depletion equivalent to five per cent (5%) of the gross income from the property, which is defined in the statute as the gross income from mining.

B. The gross income from mining in this case is the selling price of the finished brick and tile f.o.b. plant loaded

for shipment, this being the sum of $1,228,484.96. Five per cent (5%) of this figure would be a total depletion allowance of $61,424.25.

C. The Director erred in restricting the depletion allowance to five per cent (5%) of an amount arbitrarily allocated by him as mining costs, to-wit: $83,029.33, plus an amount of $13,554.06 added thereto as profits (7.86% of the total profit of the company). The base so arrived at for calculating the depletion was $96,583.39, which the Director declared to be "mining costs", and the depletion allowance of five per cent (5%) then was only $4,829.17.

D. The Director erred in refusing the full depletion allowance of $61,424.25, because the statute very clearly sets forth the fact that "mining costs" shall include all ordinary treatment processes normally applied in order to obtain the commercially marketable product, in this case, brick and tile.

E. The Director erred in refusing the requested depletion allowance in this case, because the rule applied by the Director under his regulations leads only to confusion in which the operator could never determine the exact point were mining ended and some other process began.

F. The Director erred in refusing the requested depletion allowance as being based on his regulations, because the regulations issued are contrary to the statute itself and tend a complete rewriting of the statutory language.

G. The Director erred in applying the rule set forth above and in refusing the depletion allowance, because the regulation which he purported to follow does not set forth a standard which can be readily determined, whereas it was obviously the intention of the Congress in writing the statute itself to set forth a clear standard based on the gross sales price of the first commercially marketable product, and not a calculated or imaginary value of its component products at some vaguely defined point in the train of processes beginning with the extraction of the ores and the final loading of the manufactured product.

H. The Director erred in refusing the requested depletion allowance in this case, because various courts have

construed the terms "gross income from mining" exactly as the taxpayer here has urged that it must be construed. These decisions are as follows:

(1) New Idria Quicksilver Mining Co. vs. Commissioner, 144 F. (2d) 918 (9th Cir.)

(2) International Talc Co., 15 T.C. 981

(3) Cherokee Brick & Tile Company vs. United States of America, U.S. District Court, State of Georgia, Macon Division, CA-1069 (Opinion handed down June 4, 1954).

Form ???

U. S. TREASURY DEPARTMENT
Internal Revenue Service

WAIVER OF RESTRICTIONS ON ASSESSMENT AND COLLECTION OF DEFICIENCY IN TAX AND ACCEPTANCE OF OVERASSESSMENT

Received Feb 5 1953 Int. Rev. Agent, Dallas, Texas

Pursuant to section 272(d) of the Internal Revenue Code or corresponding provisions of prior internal revenue laws, the restrictions provided in section 272(a) of the Internal Revenue Code or corresponding provisions of prior internal revenue laws are hereby waived and consent is given to the assessment and collection of the following deficiencies together with interest on the tax as provided by law; and the following overassessments are accepted as correct:

DEFICIENCIES

Type of Tax Income Year Ended December 31, 1951
Tax 9,652.89 Penalty None Total 9,652.89

Received Feb 5 1953 Int. Rev. Agt. in Charge, Dallas, Texas

RELIANCE CLAY PRODUCTS COMPANY
By /s/ George H. Harman 1-28-53

(SEAL)

Form ???

U. S. TREASURY DEPARTMENT
Internal Revenue Service

Reliance Clay Products Company
2139 North Field Street
P. O. Box 836
Dallas, Texas Dallas District

WAIVER OF RESTRICTIONS ON ASSESSMENT AND COLLECTION OF DEFICIENCY IN TAX AND ACCEPTANCE OF OVERASSESSMENT

ARC:AP:DAL
Dal:GN:90D

Holding Commissioner Received July 23 1954 Internal Revenue Appellate Division Dallas, Texas

Pursuant to section 272(d) of the Internal Revenue Code or corresponding provisions of prior internal revenue laws, the restrictions provided in section 272(a) of the Internal Revenue Code or corresponding provisions of prior internal revenue laws are hereby waived and consent is given to the assessment and collection of the following deficiencies, together with interest on the tax as provided by law; and the following overassessments are accepted as correct:

DEFICIENCIES

Type of Tax Income Year Ended 12-31-1951
Tax $37,341.47 Total $37,341.47

RELIANCE CLAY PRODUCTS CO.
P. O. Box 13226, Dallas, Texas

By /s/ G. H. Harman 7-15-54
President

Rec'd With Remittance July 16 1954 Dist. Dir. Int. Rev. Dallas Mail Unit

EXHIBIT B

Form 843

U. S. TREASURY DEPARTMENT
Internal Revenue Service
(Revised Year 1953).

CLAIM

To Be Filed With The Collector Where Assessment Was Made or Tax Paid

Received Jul 27 1956 Dist. Director Int. Rev. Dallas

Name of taxpayer or purchaser of stamps Reliance Clay Products Co. (A Corporation)

Street address P. O. Box 13,226) 2220 Shorecrest Drive

City, postal zone number, and State Dallas, Texas

1. District in which return (if any) was filed 2nd Texas.

2. Period (if for tax reported on annual basis, prepare separate form for each taxable year) from 1/1/. 1952 to 12/31/. 1952

3. Kind of tax Income.

6. Amount to be refunded as is legally refundable plus interest, including $ 3,228.61

Title 26 Code Section 114, Subsection B(4AB) provides for computation of depletion for brick and tile clay on gross income from the property instead of on the manufacturing costs.

Exhibits attached are incorporated as a part of this claim as though fully set out on this form.

Signed RELIANCE CLAY PRODUCTS CO.
/s/ J. M. Edwards
Secy

Dated July 25, 1955

RELIANCE CLAY PRODUCTS CO.
FORM 843, REFUND CLAIM
12-31-52

Net Income Per RAR, 10-28-54, by E. L. Herron		25,892.51
Plus Depletion Allowed by RAR		5,677.73
Net Taxable Income per Original 1120		31,570.34
Less: Depletion computed as follows:		
Gross Sales, RAR	1,102,338.18	
Depletion at 5%	55,116.90	
Limited to 50% of Net Profits		15,785.17
		15,785.17

INCOME TAX COMPUTATION

Net Taxable Income	15,785.17	
Income Tax at 30%		1,735.53
Assessed Per RAR, and Paid		7,964.16
Adjusted Income Tax Refund		3,228.61

Form 2??

U. S. TREASURY DEPARTMENT
Internal Revenue Service

WAIVER OF RESTRICTIONS ON ASSESSMENT AND COLLECTION OF DEFICIENCY IN TAX AND ACCEPTANCE OF OVERASSESSMENT

Received Oct. 29 1954

Pursuant to section 272(d) of the Internal Revenue Code, or corresponding provisions of prior internal revenue laws, the restrictions provided in section 272(a) of the Internal

Revenue Code or corresponding provisions of prior internal revenue laws are hereby waived and consent is given to the assessment and collection of the following deficiencies, together with interest on the tax as provided by law; and the following overassessments are accepted as correct:

DEFICIENCIES

Type of Tax	Income Tax	Year Ended	Dec. 31, 1952		
Tax	$3,228.61	Penalty	None	Total	$3,228.61

OVERASSESSMENTS

Type of Tax	Income Tax	Year Ended	Dec. 31, 1951		
Tax	$8,619.47	Penalty	None	Total	$8,619.47

Reliance Clay Products Company,
P. O. Box 13226,
Dallas, Texas.

By /s/ George H. Harman 10/28/54

(SEAL)

"Exhibit C"

U. S. TREASURY DEPARTMENT
Internal Revenue Service
District Director
Dallas, Texas

January 13, 1956

In Replying Refer to:
Code 1120

Reliance Clay Products Co.
Box #13,226
Dallas, Texas

Amount of claim: $37,341.47
Taxable period: 1951

In accordance with the provision of Section 6532 (a) (1) of the Internal Revenue Code, notice of disallowance of your claim in full is hereby given by registered mail.

By direction of the Commissioner.

Very truly yours,

s/ Ellis Campbell, Jr.
Ellis Campbell, Jr.,
District Director

FL-74
IRS - Dallas, Texas

"Exhibit D"

U. S. TREASURY DEPARTMENT
Internal Revenue Service
District Director
Dallas, Texas

January 13, 1956

In Replying Refer to:
Code 1120

Reliance Clay Products Co.
Box 13,226
Dallas, Texas

Amount of claim: $3,228.61
Taxable period: 1952

In accordance with the provision of Section 6532 (a)(1) of the Internal Revenue Code, notice of disallowance of your claim in full is hereby given by registered mail.

By direction of the Commissioner.

Very truly yours,

s/ Ellis Campbell, Jr.
Ellis Campbell, Jr.,
District Director

FL-74
IRS - Dallas, Texas

ANSWER

Filed April 9, 1956.

Comes now the United States by its attorney, Heard L. Floore, the United States Attorney for the Northern District of Texas, and answers the allegations of the complaint as follows:

1, 2, 3, 4, 5. Admits the allegations of paragraphs 1, 2, 3, 4 and 5 of the complaint.

6. Admits the allegations of paragraph 6 of the complaint. Defendant alleges that plaintiffs paid the income tax liabilities shown on said returns of the following dates:

(a) Calendar year 1951 Return:

$13,086.36	on March 12, 1952
24,303.24	on June 10, 1952
$37,389.60	

(b) Calendar year 1952 Return:

$ 1,895.55	on March 17, 1953
1,420.00	on June 15, 1953
1,420.00	on August 12, 1953
$ 4,735.55	

7. Admits the allegations of paragraph 7, (a) and (b), of the complaint, but denies that the said Revenue Agents' Reports dated February 2, 1953 and October 28, 1954, allowed plaintiff a deduction for percentage depletion in the manner paraphrased by plaintiff's paragraph 22 of the complaint (the complaint is in error by reference to paragraph 21 of the complaint for said Agents' Reports).

8. Admits the allegations of paragraph 8 of the complaint.

9. Admits the allegations of paragraph 9 of the complaint. Defendants alleges with respect to the allegations of paragraph 9(a) of the complaint that the sum of $10,215.53 was received by the Commissioner on April 6, 1953, that the sum of $37,341.47 was received on July 16, 1954, and the sum of $5,233.94 was received on August 23, 1954.

10. Admits the allegations of paragraph 10 of the complaint, but it is not intended to admit any of the allegations contained in plaintiff's claims for refund for 1951 and 1952, attached to the complaint as Exhibits A and B, not expressly admitted elsewhere in this answer.

11, 12, 13. Admits the allegations of paragraphs 11 12 and 13 of the complaint.

14, 15. Denies the allegations of paragraphs 14 and 15 of the complaint for the reason that the applicable sections of the Internal Revenue Code of 1939 speak for themselves.

16. Denies the allegations of paragraph 16 of the complaint, but admits that the term "brick and tile clay" as used in Section 114(b)(4)(A) of the Code means clay used or sold for use in the manufacture of common brick, drain and roofing tile, sewer pipe, flower pots, and kindred products.

17. Denies the allegations of paragraph 17 of the complaint, but admits that Section 29.23(m)-5 of Treasury Regulations 111, as amended by T.D. 6031, approved July 14, 1953, defines clay, brick and tile, as follows:

> Clay used or sold for use in the manufacture of common brick, drain and roofing tile, sewer pipe, flower pots and kindred products (other than clay specifically identified as a clay for which a 15 percent rate of percentage allowance is provided).

18. Defendant lacks knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 18 of the complaint.

19. Denies the allegations of paragraph 19 of the complaint.

20. Defendant is without knowledge or information sufficient to form a belief as to the truth of the allegations of pargraph 20 of the complaint, except it is denied that all of the steps (a) through (m) are "processes" within the meaning of Section 114(b)(4)(B) of the Internal Revenue Code of 1939.

21. Admits the allegations of paragraph 21 of the complaint, but denies that the selling price of $1,000,788.47 for 1951 or $851,031.27 for 1952 is the subject for depletion within the meaning of Section 114(b)(4)(A) and (B) of the Internal Revenue Code of 1939.

22. Denies the allegations of paragraph 22 of the complaint, but admits that the figures quoted and their manner of classification are accurate, that the revenue agents calculated the percentage figures for allocation of administrative costs and profits to the three phases, mining, manufacturing, and selling, of plaintiff's business for 1951 and the same phases for 1952 but including a new phase, "handling" and "other expenses", and further admits that the Revenue Agents' Report for 1951 took 5 per cent of $96,583.39 to arrive at depletion ($4,829.17) and for the year 1952 took 5 per cent of $113,554.68 to arrive at depletion ($5,677.73).

23, 24, 25. Denies the allegations of paragraphs 23, 24 and 25 of the complaint.

26. Denies the allegations of paragraph 26 of the complaint, but admits no part of the sums of $22,944.20 and $3,228.61 have been credited, remitted, refunded or repaid to the plaintiff or to anyone on its account.

WHEREFORE, defendant demands judgment in its favor, with allowable costs.

s Heard L. Floore
Heard L. Floore
United States Attorney

s John C. Ford
John C. Ford, Assistant
United States Attorney

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Witness	Direct	Cross	Redirect	Recross
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PLAINTIFFS:

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IN THE
DISTRICT COURT OF THE UNITED STATES
FOR THE NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION

RELIANCE CLAY PRODUCTS COMPANY,
VS. NO. 6400, Civil
UNITED STATES OF AMERICA

* * *

BE IT REMEMBERED that on the 12th day of May, 1956, before the Honorable William H. Atwell, United States District Judge, the following proceedings were had in the above styled and numbered cause:

* * *

APPEARANCES:

TURNER, RODGERS, WINN, SCURLOCK & TERRY, Dallas, Texas,
By Mr. George S. Terry, and
Mr. Charles D. Turner,
appearing for the plaintiff;

MR. JOHN C. FORD, Dallas, Texas,
MR. GERARD O'BRIEN, Washington, D. C.
appearing for the Defendant.

PROCEEDINGS

THE COURT: All right. Call your first witness, Gentlemen.

MR. TERRY: We first want to offer a stipulation which we call Stipulation of Facts Number 1.

I will ask the court reporter to mark it.

(The instrument referred to was here marked Plaintiff's Exhibit Number 1, for identification.)

THE COURT: You read it to me if you want me to hear it.

MR. TERRY: All right, sir.

I would like permission to read this stipulation in part, and state certain paragraphs—

THE COURT: How is that?

MR. TERRY: I would like to read part of it verbatim and to summarize portions of it, Your Honor.

THE COURT: Well, I don't know what your stipulation is; you and the counsel stipulated those as facts.

MR. TERRY: I would like to read that for you.

THE COURT: I say: Have you and the counsel stipulated?

MR. TERRY: Yes, Your Honor.

THE COURT: Well, is there any provision in there for just reading part of it?

MR. TERRY: No, sir, unless he is agreeable to it; I will be glad to read it all.

THE COURT: You introduced certain parts of it?

MR. TERRY: I want to introduce it all, Your Honor.

THE COURT: All right, then, you have to read it all. Supose you stand up there so I can hear you.

MR. TERRY: All right.

THE COURT: Right there is all right.

MR. TERRY: "It is hereby stipulated and agreed by and between the parties hereto, by their respective counsels, that the facts hereinafter stated shall be taken as true, provided, however, that this stipulation shall be without prejudice to the right of either party to introduce upon the trial of this case any other and further evidence not inconsistent with the facts herein stipulated:

1.

"Plaintiff brings this action against defendant pursuant to Section 1346(a)(1) of Title 28 of the United States Code, Act of June 25, 1948, c. 646, 62 Statute 869, 933, as amended by the Act of May 24 1949 c. 139, Paragraph 80(a), 63 Statute 89, 101, as amended by the Act of July 30, 1954, c. 648, 1, 68 Statute 589.

2.

"This action is brought by Reliance Clay Products Company for the recovery of:

"(a) $22,944.20 of income tax and interest thereon as provided by law for the calendar year 1951; and

"(b) $3,228.61 of income tax and interest thereon as provided by law for the calendar year 1952."

THE COURT: Now, you gentlemen call that a stipulation of facts?

MR. TERRY: Well, there is quite a little to it, Your Honor.

THE COURT: We try to summarize here and get down to the facts of a case, but without repetition, you know. You have just told me what the suit is about and I can look on the docket and see what it is about.

Have you got some stipulations as to facts in this case?

MR. TERRY: Yes, sir.

THE COURT: Well, let's hear them now.

MR. TERRY: We have stipulated that within the time prescribed by law the plaintiff made and filed its income tax returns showing the income tax liability as shown on those forms, and that pursuant to such Revenue Agent's Report for 1951 the Commissioner made an additional assessment of $9,652.89 of income tax and of $562.64 of interest thereon representing additional amounts due set out therein, and

that these amounts were duly paid to the Commissioner, and on July 27, 1955, plaintiff duly filed with the District Director of Internal Revenue for the Second District of Texas at Dallas, Texas, a claim for refund of income taxes for 1951, and also a claim for refund of income taxes for 1952.

These two separate claims represented the additional amounts paid for the adjustments to depletion pursuant to such additional assessments referred to in Paragraph 9.

It is agreed that if plaintiff is entitled to a deduction for depletion on its gross income from mining as computed by the Internal Revenue Agent, and as alleged in Paragraph 13, the accounting method and the depletion deductions as computed pursuant thereto for the calendar years 1951 and 1952 are correct. If plaintiff has overpaid its income taxes based on plaintiff's method of computation of gross income from mining, based on five per cent of the sales price of its brick and tile clay, f.o.b. plant, loaded for shipment, the plaintiff has overpaid its income taxes in the amount of $22,944.20 for 1951 and in the amount of $3,228.61 for 1952.

Then, it is agreed that the following processes are applied by plaintiff to the mineral product clay in order to manufacture burnt brick or tile which are sold by the plaintiff:

First, the clay is mined by a dragline and loaded in dump-trucks which carry the clay to a nearby plant

b) The clay taken to the plant is sometimes thered in a storage shed.

c) The clay is either dumped directly from the np truck or is taken from the storage shed and ed in a feeder from which the clay passes into a pan crusher, which crushes and grinds the clay.

d) The clay is discharged from the dry pan sher on to the elevator belt which carries it to creen.

e) The clay passes through the screen into a bin; m the bin the clay passes into a feeder.

f) The clay is discharged from the feeder into pug mill, which is a machine wherein water is ed as the final tempering process.

g) From the pug mill the clay passes into the k or tile machine. It first goes into an evacuation mber where air is evacuated from the clay by a uum pump. The clay then passes into the extru- n section of the machine where it is forced under ssure through various types of dies in long ribbons.

h) The long ribbons of clay as extruded through dies pass into the cutting machine which cuts them clay units of desired size.

i) The clay units as cut pass on to a conveyor and are then stacked on to dryer or kiln cars which moved to the dryer tunnels or to the continuous nnel-Kiln, where free water is evaporated from the y units by open gas fires, or waste heat from kiln.

(j) When the free water is thus removed the clay units are either stacked in periodic kilns, or in the case of continuous or tunnel-kilns, are left on the kiln cars which continue from the dryer to the kiln.

(k) The clay units are then burned by natural gas fires whether in periodic or continuous (tunnel) kilns.

(l) The burnt brick and tile is then removed from the kilns.

(m) After it has been removed from the kilns the burnt brick and tile is either stacked on the yard or loaded directly for shipment to purchasers.

Now, we have agreed that for these processes the Commissioner computed his tax from the first six and refused the last eight. I believe that is the substance of that stipulation, Your Honor. We offer it in evidence.

THE COURT: All right.

MR. TERRY: We next offer in evidence—

Will you mark this?

(The instrument referred to was here marked Plaintiff's Exhibit Number 2, for identification.)

MR. TERRY: We next offer in evidence as Plaintiff's Exhibit Number 2 a document styled "Stipulation of Facts Number 2", entered into between the plaintiff and the defendant.

Now, this Stipulation of Facts contains all of the details of a nationwide survey which was made by the government with respect to a possible market for clay in a raw state, and without reading that portion which is not a stipulation of fact I would like to state that this stipulation shows the following:

It shows a total of 674 establishments in the United States producing brick and hollow tile. It shows that there is, for the years 1951, '52 and '53, an annual average of national production of clays of all types, both fire clay and brick and tile clay, of 22,000,000 tons, of which only .87 of 1% was sold in its raw state, before they were burnt into a finished product and if you leave out the strictly fire clay and go to the brick and tile clay only, this stipulation shows that there was, in those three years an average round figure of 18,000,000 tons of brick and tile clay, of which only 113,000 tons were sold, and all of those but 16,000 were sold intercompany sales, sales of that character, sales between unrelated parties amounted to only 16,177 tons, .09 per cent sold in its raw state, aside from the manufactured, finished products.

We offer Plaintiff's Exhibit Number 2 in evidence.

We would like to call Mr. Edwards, Your Honor.

THE COURT: All right.

J. B. EDWARDS,

the witness hereinbefore named being first duly sworn to testify the truth, the whole truth and nothing but the truth, testified on his oath as follows:

DIRECT EXAMINATION

BY MR. TERRY:

Q. Mr. Edwards, please state your name.

A. J. B. Edwards.

Q. Where do you live, Mr. Edwards?

A. 3424 Cornell, Dallas.

Q. What business are you in?

A. Brick and tile.

Q. With what company are you associated?

A. With the Reliance Clay Products.

Q. What is your official connection with that company?

A. Secretary and Treasurer.

Q. How long have you been Secretary and Treasurer of Reliance Clay Products Company?

A. Since 1942.

Q. How many plants does that company operate?

A. Two.

Q. Where?

A. At Mineral Wells and Lindale, Texas.

Q Now, what products do you manufacture out of the tile—out of the clay that you produce?

A Brick and tile, structural brick and tile.

Q Are you thoroughly familiar with the processes that have just been read from the stipulation here that are used in your plants to make brick and tile?

A I am.

Q I want to ask you what is the first commercially marketable mineral product that you have in your plant?

A The finished bricks.

Q Now, is there any point in any of these thirteen named processes, from the first up to until you get to the finished brick where you have a product that is a commercially marketable product?

A There is no market for any of it until it is completed, the processes are completed.

Q Now, you are familiar also with the sales of your plant, are you not?

A Yes, sir.

Q Do you sell any brick and tile clay that you mine in its raw, unmanufactured form?

A We do not.

Q Is there any market for it, as far as you know?

A As far as I know, there is none.

Q Are you an officer of any national brick and tile manufacturers organization?

A I am.

Q What is that organization?

A The Structural Clay Products Research Foundation.

Q Where is its principal office?

A In Chicago.

Q What is your office with it?

A I am a director.

Q How long have you been a director?

A Approximately four years.

Q As such a director in connection with research in the brick and tile industry, have you had occasion to travel throughout Texas, to the brick and tile plants in Texas?

A. I have.

Q Have you, at my request, made up a computation of how many brick plants you have been in in Texas?

A I have.

Q How many?

A Approximately 40 or 45.

Q From your knowledge, do you know whether or not any of these plants that you have been in sell any

of this raw clay in its unmanufactured or unfinished form?

A None that I have been in.

Q Have you ever been in that little plant out in Snyder, Texas?

A No, sir.

Q Do you know from something that they do have a small sale.?

A I heard in this court that they did, at a prior hearing.

Q In this stipulation which is offered in evidence here it is shown that that plant in Snyder, Texas had a sale of 78 tons of raw clay at cost, as an accommodation to a friend, in 1954, and 520 tons in 1955, again at cost, for the accommodation of a friend.

About how many—in terms of little, small, average homes, how many houses would 78 tons of brick build?

A Between three and four homes.

Q How many tons of brick—how many tons of clay do you produce annually, on an average, in your plants?

A Above forty million bricks, not tons; that would be approximately 80,000 tons.

Q All right. In terms of homes, about how many of that same type of small home would your annual production build? Have you got a calculation on that?

A Between four and five thousand annually.

Q. Also in connection with your job in connection with the National Structural Clay Products Research Laboratory, have you had occasion to travel throughout the United States?

A. I have.

Q. How many different states have you traveled in and studied the processes and sales in brick plants?

A. Fifteen.

Q. And from your knowledge of your travels to those different plants, have you not found any of those plants that have any market for clay in its raw, unfinished form?

A. None.

MR. TERRY: I believe that is all.

THE COURT: Any cross, Counsel?

MR. O'BRIEN: Yes, Your Honor.

* * *

CROSS EXAMINATION

BY MR. O'BRIEN:

Q. Mr. Edwards, are you acquainted with the fact that clay is marketed in the United States?

A. Some types of clays.

Q. Is brick and tile clay, as is manufactured for brick and tile use, marketed in the United States?

A. None that I know of.

Q Are you aware of this stipulation entered into by the parties showing sales of clay in the United States, of brick and tile clay?

A I have read that.

Q Have you ever heard that in the year 1951 the sales of brick and tile clay with the cone equivalent of under 15 had reached as much as 150,000 - 152,000 tons?

A I have read that; I don't know of any sales of that amount, no, sir.

Q Are you aware of the fact that over a five year period from 1951 to 1955, that over a half million tons of clay, brick and tile clay, has been sold in the United States for the manufacture of brick and tile?

A I am not aware of that fact.

Q Has your Structural Clay Products Institute ever investigated the sales of brick and tile clay in the United States?

A Not specifically.

Q They have never issued—

THE COURT: Speak where I can hear you. Not specifically?

THE WITNESS: Not specifically, no, sir.

THE COURT: All right.

MR. O'BRIEN: Excuse me, Your Honor.

THE COURT: Go ahead.

Q (By Mr. O'Brien) Are you aware of the fact that the Bureau of Mines computed the sales of brick and tile clay in the United States for the year 1951 in the sum total of 84,402 tons?

A I am not aware of the fact.

Q Are you aware of the fact that from 1952, that total jumped to 230,295 tons; and for the year 1953 it increased to 342,506 tons?

THE COURT: Answer out.

A No, I am not aware of it.

THE COURT: You see, you can't shake your head; the reporter doesn't get it then.

THE WITNESS: Yes, sir.

Q (By Mr. O'Brien) How far is it from your plant at Mineral Wells, Texas to Denver, Colorado?

A I do not know.

Q Would you say it was approximately 700 miles?

A Something on that order.

Q Are you in Mineral Wells closer to Denver, Colorado than say, Brazil, Indiana?

A I am not aware of the distances.

Q Would you say that Brazil, Indiana was approximately a thousand miles away from Denver, Colorado?

A I do not know.

THE COURT: What is your answer?

THE WITNESS: I don't know the distances.

THE COURT: You don't know?

THE WITNESS: No, sir.

Q (By Mr. O'Brien) Do you know if it is a greater distance from Indiana to Colorado than from Texas to Colorado?

A I don't know the distances.

Q Have you ever traveled to Colorado?

A I have been there once.

Q Are you acquainted with the fact that in the State of Colorado that clay purchased through the years 1951 through 1955 had totaled approximately 350,000 tons?

A I am not aware of the fact. For what purpose was this clay purchased?

Q For brick and tile purposes, for terra cotta. You are not aware of that?

A No.

Q If you had the opportunity—

A I have been on one Colorado plant and they were not purchasing their clay.

Q Do you know that Denver Terra Cotta Company purchases clay, and the Denver Brick and Pipe Company purchases clay?

THE COURT: Answer out; answer out; answer out.

A I have never been on those two places.

THE COURT: Well, just say "No", "No", "No", if that is your answer, or "Yes", "Yes", "Yes".

Q (By Mr. O'Brien) Do you think it would be profitable for you to engage in the marketing of clay in the State of Colorado from Texas?

A No, sir.

Q Are you aware of the fact that Brazil, Indiana producers of brick and tile clay do ship to Colorado for purposes of selling their clay?

A No.

THE COURT: All right.

MR. O'BRIEN: That is all.

THE COURT: Call your next witness, please.

MR. TERRY: That is all for us, Your Honor please. Plaintiff rests.

MR. O'BRIEN: Your Honor, the government would like to read a part of the stipulation that we feel is essential to our case, entered into by the parties in this proceeding.

THE COURT: Well, has it been read?

MR. O'BRIEN: No, it has not been read, Your Honor.

THE COURT: All right.

MR. O'BRIEN: Paragraph 16 of the stipulation

"Of the above processes the Commissioner has included in the computation of gross income from mining as applied by plaintiff to the mineral product clay in order to manufacture burnt brick and tile, the following:

A Costs of extraction:

(a) Dragline operation by which the clay is extracted from the pit.

(b) Loading of the bulk clay in dump trucks which carry the clay to a nearby plant.

B Costs of treatment:

(a) Dumping of the trucks loaded with clay into the storage shed where the clay is weathered.

(b) Placing the clay into a feeder from which the clay passes into a crusher.

(c) The dry pan crusher which crushes and grinds the clay.

(d) The clay is discharged from the dry pan crusher on to an elevator belt which carries it to a screen, from whence it passes through the screen to a storage bin.

17.

"The following processes the Commissioner has not included in the computation of gross income from mining. It is the government's contention that all processes applied to the mineral product clay in this paragraph are not mining treatment processes but manu-

the form in which it emerged from the mine. It is the taxpayer's—"

THE COURT: Just a moment, please, Counsel. This, you said, was in the stipulation between the parties?

MR. O'BRIEN: It is in the stipulation, Your Honor.

THE COURT: That is what I wanted to know.

MR. O'BRIEN: "It is the taxpayer's contention that all of the processes in this paragraph are ordinary treatment processes within the meaning of Section 114(b)(4)(B) of the Internal Revenue Code of 1939."

Those following processes which the Commissioner considers to be manufacturing, are these:

"(a) The clay which has been screened is picked up by the feeder and discharged, into the pug mill, which is a machine wherein water is added as a final tempering process.

"(b) From the pug mill the clay passes into the brick or tile machine. It first goes into an evacuation chamber where air is evacuated from the clay by a vacuum pump. The clay then passes into the extrusion section of the machine where it is forced under pressure through various types of dies in long ribbons.

"(c) The long ribbons of clay as extruded through the dies pass into the cutting machine which cuts them into clay units of desired size.

"(d) The clay units as cut pass on to a conveyor belt and are then stacked on to dryer or kiln cars which are moved to the dryer tunnels or to the continuous tunnel-kiln, where free water is evaporated from the clay units by open gas fires, or waste heat from kiln.

"(e) When the free water is thus removed the clay units are either stacked in periodic kilns, or in the case of continuous or tunnel-kilns, are left on the kiln cars which continue from the dryer to the kiln.

"(f) The clay units are then burned by natural gas fires whether in periodic or continuous tunnel kilns.

"(g) The burnt brick and tile is then removed from the kilns.

"(h) After it has been removed from the kilns, the burnt brick and tile is either stacked on the yard or loaded directly for shipment to purchasers."

I would also like to read from Stipulation Number 2 these figures.

MR. TERRY: What page?

MR. O'BRIEN: Number 6. Part 1 of the stipulation, page 6.

For the year 1951; total tons sold, that includes all clay which is sold for use in the manufacture of brick and tile products. For the year 1951 it is 252,496.66 tons. The total value for that clay amounted to $465,629.82.

For the year 1952, total tons sold amounted to 298,949.25 tons. The total value of tons sold amounted to $631,356.38.

For the year 1953, total tons sold, 402,646.92 The total value for the tons sold, $766,996.25.

Total tons sold for the year 1954, 445,178.43. Total value of tons sold, $673,753.39.

And lastly, for the year 1955, total tons sold reached 512,358.50 tons, for a total value of $1,016,133.62.

Part 1 also breaks down for the years 1951 through 1955 clay which has a pyrometric cone equivalent of under 15 and clay which has a pyrometric cone equivalent of over 15, and some clay on which the pyrometric cone equivalent is unknown.

If I might inform the Court, the pyrometric cone equivalent would indicate the clay that is capable of being used for fire or refractory products. It is generally acknowledged that if it is over 15, that ratio of over 15 would indicate it could be used for fire or refractory products. For that clay which would not be used for fire and refractory products, the sum total for the years of '51 through '55 amount to 550,933 tons.

Of the clay that would be used for fire and refractory purposes, but here it was channeled into brick and tile, and was over 15, amounted, for the sum total of 15 to 18—excuse me—amounted to the sum total of 111,053 tons.

For P.C.E. over 15, it amounted to 1,229,878.86 that went into the manufacture of brick and tile.

MR. TERRY: Where are you reading that?

MR. O'BRIEN: P.C.E. Unknown totaled 19,764.9.

And the grand total for all clay which has gone into the manufacture of brick and tile, whether it be under 15 or over 15, has amounted to 1,911,629.76 tons.

The Bureau of Mines Reports, from questionnaires received from producers of brick and tile clay, that for the year 1951, total tons sold was 84,402.

For the year '52, 230,295.

For the year '53, 342,506.

THE COURT: Is that in your stipulation also?

MR. O'BRIEN: That is the stipulation, the Bureau of Mines Report. The Bureau of Mines Report showed that the average price of the clay reported to them in the questionnaires from the producers of brick and tile clay amounted to $1.24 for the year 1951, $1.10 for the year 1952, and for the year 1953, $1.62.

At this time the government would like to call Mr. Fiske.

* * *

L. E. FISKE,

the witness hereinbefore named, being first duly sworn to testify the truth, the whole truth and nothing but the truth testified on his oath as follows:

DIRECT EXAMINATION

BY MR. O'BRIEN:

THE COURT: F-i-s-k (spelling)?

THE WITNESS: F-i-s-k-e (spelling).

Q (By Mr. O'Brien) Will you please state your name?

A Leland E. Fiske.

Q What is your address?

A Dallas.

Q What is your occupation?

A I am Reviewing Engineer for the Internal Revenue Service in the Dallas region.

Q What is your academic background?

A I graduated from the University of Kansas in 1916 with a B.S. degree in mining engineering.

Q Do you have any other degrees?

A No.

Q Mr. Fiske, what is clay?

A Well, clay is a mineral that is produced by the decomposition of various rocks.

THE COURT: You will have to speak out, now, so we can hear you. Decomposition of what?

THE WITNESS: Various rocks.

THE COURT: Various rocks?

THE WITNESS: Rocks, yes, Your Honor.

Q (By Mr. O'Brien) What are those rocks generally called?

A They are called minerals.

Q Is clay, then, a composite of minerals?

A Yes.

Q Is clay—well, tell us how is clay formed in nature?

A It is formed by the gradual decomposition of these various rocks.

Q How long does decomposition take?

A Well, it takes many, many years.

Q Well, how many?

A Oh, in the thousands of years.

Q What are some of the impurities that clay contains?

A Well, one of the principal impurities is sand, silica.

Q Is carbon an impurity?

A Yes.

Q Iron?

A Yes.

Q Sulphates?

A Yes.

Q Do any of these impurities affect the product which can be made from the clay?

A Yes.

Q What is the pyrometric cone equivalent of clay? What is meant by that term?

A Well, it determines the use of the clay for refractories, that is, in order to be used as a refractory it has to have a high pyrometric cone equivalent; it is the test that is used to determine whether or not clay can be used for refractories, for fire clay products.

Q If clay had a high pyrometric cone equivalent but also a great deal of impurities, say iron or carbon or sand, could it still be used for fire or refractory purposes?

A No, not if it had too much impurity.

Q If I showed you clay which could be used for the manufacture of, say, fire or refractory products, and clay which could be used for common building brick and tile, would you be able to distinguish the clays by sight or by feel?

A Usually not.

Q Is it generally true that the only way that the

tell whether the product will be successful or not is to shape it or form it into the product and subject it to the normal heat processes?

A Yes, that is the usual way of testing it.

Q It is true that in order to compensate for the impurities in clay that the manufacturers of clay products will buy clay in order to mix with their own clay deposits?

MR. TERRY: I object to that as calling for a conclusion.

THE COURT: Yes, I don't see how—hardly how he would know about that.

Q (By Mr. O'Brien) Mr. Fiske—

THE COURT: Try your question again. You can see the fault in it, can't you?

MR. O'BRIEN: Yes, Your Honor.

THE COURT: All right.

Q (By Mr. O'Brien) In order to compensate for defects or impurities that might exist in clay, what do clay producers generally do?

MR. TERRY: I object unless he lays a predicate to show that he knows what clay producers generally do. He is an expert and can testify about clays; but I don't know about this "what clay producers generally do".

MR. O'BRIEN: I will qualify him.

Q (By Mr. O'Brien) Do you know of your own knowledge and experience of the industry what is done?

A Yes, in a general way.

Q Will you state what it is?

A Well, if the producer doesn't have a clay that will meet the specifications of the product he wants to make he usually acquires some other clay and blends it with it until he gets the proper clay.

Q Would the blending accomplish different colors in the end product?

A Yes.

Q Mr. Fiske, after a brick is made in the kiln if you ground that brick up what would be the name for the pulverized material from the ground brick?

A I think I have forgotten that term.

Q If I might remind you—

THE COURT: Speak out so I can hear you.

THE WITNESS: I say that I think I have forgotten the term.

A Is it grog?

Q (By Mr. O'Brien) Yes.

If you mixed grog with water would you have clay?

A No.

Q If you mixed grog with water and put it into a clay—excuse me—into a brick machine, would you be able to make a brick out of it?

A No.

Q Is there a distinction then, between the clay which goes into the brick and the grog which becomes the brick?

A Yes.

Q Is there a chemical distinction?

A I think probably a chemical change takes place; at least, there is a cementing there that changes the character of the material.

Q Would you say that brick is a product made out of the mineral clay?

A Yes, brick is made from clay.

Q In that sense, it is a mineral product, is that the case?

A I don't think that brick is a mineral product; I think the brick is a manufactured product made out of a mineral.

Q Why do you say it is a manufactured product made out of mineral?

A Because it has to go through manufacturing processes, molding and shaping and firing.

Q What do those processes accomplish?

A They accomplish the manufacture of a brick.

Q. Well, do they change the form of the clay in any way?

A. They change its form, and change it from a loosely consolidated material into a solid brick, into a rock.

Q. Have you ever heard of the sales of brick and tile clay?

A. Yes.

Q. For use in the manufacture of brick and tile products?

A. Yes, I know that there are some sales.

Q. Are you acquainted with the stipulation entered into by the parties to this proceeding?

A. I have read the stipulation.

Q. Do you believe that the sales of brick and tile clay, as shown by the stipulation, are rather considerable?

MR. TERRY: I object to that; the stipulation would show what they are, Your Honor.

THE COURT: I suppose the Court would have to pass on that; he can tell what the stipulation is, and he has already done that.

MR. TERRY: Yes.

Q. (By Mr. O'Brien) Do you, as a mining engineer, understand generally what is meant by the term

A Yes.

Q Would you state what that is?

A Well, mining refers to the removing of the mineral from the mine.

In clay practice it is largely a quarrying operation; it is the digging of the clay out of its natural formation and making it available.

Q After the clay has been extracted from the quarry, or any other mineral which has been extracted from a mine, do miners generally apply some sort of treatment processes?

A Yes.

Q To the mineral product?

A Yes.

Q If they wish to extract metal from the mineral which is extracted from the mine, what are the general processes by which that is accomplished?

MR. TERRY: Unless he says what metal. I don't see—

THE COURT: I don't see any relevancy of that here.

MR. O'BRIEN: Well, I will ask this question, Your Honor. This will be my last.

Q (By Mr. O'Brien) Are those processes by which you extract a metal from the mine, as mentioned in

of extraction now, do they at all change the form of the metal from that which it emerges from the mine?

MR. TERRY: I object again. The question about metals has nothing to do with this case, Your Honor; it is irrelevant and immaterial what it does with metals; this is brick and tile clay.

THE COURT: Well, you can cross examine him if you want to. I think he has a right to answer that.

MR. TERRY: All right, Your Honor.

THE COURT: I don't see the relevancy quite.

MR. O'BRIEN: Yes, Your Honor.

If I might have an answer, we hope to show the relevancy.

A You are asking about the processes beyond the ordinary treatment processes?

Q (By Mr. O'Brien) No, no, I am not.

A You are asking about the ordinary treatment processes?

Q For extraction, yes.

A No, they make no change in the mineral; they merely remove impurities and put it in a shape where it can be marketed.

Q Now, generally, after a miner has extracted his mineral product he is either going to sell it in its crude form or he is going to attempt to extract some sort

of metal from the crude mineral which he has extracted, is that generally the case?

A Yes.

Q And none of those operations, to your knowledge, ever change the basic form of the mineral from that in which it emerged from the mine?

A No.

THE COURT: All right.

MR. O'BRIEN: That is all. Thank you.

THE COURT: Any cross?

MR. TERRY: Yes, sir, Your Honor.

* * *

CROSS EXAMINATION

BY MR. TERRY:

Q Mr. Fiske, you say that insofar as these metals and other things you were talking about just now are concerned that the mining processes you are talking about are merely those that are necessary to put it in shape so it can be marketed?

A Usually, yes.

Q Yes, sir. Now, I want to ask you about one other thing:

Whenever this brick, this clay is manufactured into brick and tile, you say it is a mineral when it starts, it is a composite mineral, isn't it?

A Yes.

Q And when it gets to be just before it is fired it is still that composite mineral, isn't it?

A Yes, with the addition of water.

Q All right. But with the addition of water it is the same composite mineral just as it came out of the ground before it is fired, isn't it?

A Yes.

Q Aren't those same minerals still in it after it has been fired to make brick and tile?

A It has been changed from clay to a rock.

Q But it still has those same composite minerals it had in it before it went into the kiln to be fired?

A Still has the same chemical compounds.

Q You say that when you grind up a brick you have grog?

A Yes.

Q Does that not have the same mineral consistency?

A You can't make bricks out of it.

Q Is that a distinction between the clay mining process and the manufacturing process, if you grind up a product, you can't make it into brick again?

A To me it is.

A Yes.

Q So, you can make a brick out of it if you add a little more fresh clay with it?

A You can add a small amount of grog to clay and make bricks.

Q All right. This pyrometric cone equivalent, just for the---what is that?

A pyrometric cone is just what it implies; just a little clay cone?

A That is right.

Q Isn't it just a sort of thermometer device?

A Yes.

Q Am I holding in my hand three of these pyrometric cones?

A Yes.

Q What happens to these cones when you reach a certain heat?

A They fall over.

Q Fall over like this one?

A That is right.

Q That is like you had an expensive thermometer that says when you reach 2500 degrees Farenheit?

A That is right.

Q So, this pyrometric cone is just like saying you fire a clay to a certain heat to get the required effect, is that right?

A Yes, sir.

Q Is that right?

A Yes, sir.

MR. TERRY: I believe that is all, Your Honor.

THE COURT: All right. Call your next witness.

MR. O'BRIEN: That is all for the government, Your Honor.

MR. TERRY: I have a rebuttal, one line of rebuttal testimony, Your Honor, from Mr. Edwards, if I may.

THE COURT: How is that?

MR. TERRY: I want to recall Mr. Edwards for a rebuttal testimony.

THE COURT: I can't hear you.

MR. TERRY: I want to call Mr. Edwards for two questions of rebuttal.

Come back, Mr. Edwards.

J. B EDWARDS

being recalled to the stand, testified on his oath as follows:

DIRECT EXAMINATION

BY MR. TERRY:

Q Mr. Edwards, you heard Mr. Eiske just testify about what grog was, did you not?

A Yes, sir.

Q Do you have in your manufacturing process any of that grog?

A Yes, sir.

Q That is just a ground up brick?

A Yes, sir.

Q You put that—you use that in making other bricks?

A Yes, sir.

Q Do you have with you here—what is this that you have in your hand?

A That is a sample of a brick containing grog.

Q What percentage of grog?

A Approximately ten per cent.

Q Ten per cent grog and ninety per cent fresh clay?

MR. TERRY: That is all.

THE COURT: All right. Any cross?

MR. O'BRIEN: No, Your Honor.

THE COURT: All right. Both sides close?

MR. TERRY: We close, Your Honor.

* * *

THE COURT: This suit was filed on February 8th of the present year. Summons was executed on February 8th, and answer was filed on April 9th, giving the government statutory time for service and for answer.

I find the facts to be as stipulated, and also in addition to those facts, I find from the oral testimony of witnesses that the clay which enters into the manufactured product, tile and brick, goes through a process before it becomes merchantable; that the de minimis sales disclosed in the testimony are not influential in the change of the statute or in the regulation of the Commissioner himself.

I think some sales are de minimis, and that the plaintiff is entitled to recover judgment for the amount set forth in the stipulation and the added interest also set forth there.

* * *

I, RICHARD A. WARD, certify that during the trial of the foregoing styled and numbered cause, I

and the proceedings on said trial and have transcribed the same as shown by the above and foregoing pages, and that said transcript is true and correct.

This 14th day of June, A.D. 1956.

s/ Richard A. Ward
(Richard A. Ward)
Court Reporter.

FINAL JUDGMENT

Filed May 15, 1956

On the 12th day of May, A.D. 1956 came on to be heard the above entitled and numbered cause and came the parties by attorneys and by written pleadings, and no jury having been demanded all matters both of fact and of law were submitted to the Court without the intervention of a jury.

The Court having heard the evidence of the parties and having heard argument of the attorneys after both parties plaintiff and defendant each announced that they closed their case and being of the opinion that the facts and law are in favor of the plaintiff and against the defendant, and that the plaintiff is entitled to a judgment for refund of taxes as prayed for in its complaint for the calendar years 1951 and 1952.

It is therefore ORDERED ADJUDGED AND DECREED that the plaintiff, Reliance Clay Products Company, do have and recover of and from the United States of America the following sums:

(a) $22,944.20 for the calendar year 1951; and

(b) $3,228.61 for the calendar year 1952, with

(c) Interest on each amount, as provided by law, together with its costs of suit.

To which action of the Court the defendant, The United States of America, in open Court excepted.

RENDERED AND ENTERED this the 15 day of May, A.D. 1956.

s/ Wm. H. Atwell
U. S. Dist. Judge

APPROVED AS TO FORM:

s/ John G. Ford
Attorney for Defendant

STIPULATION OF FACTS NO. 1

IT IS HEREBY STIPULATED AND AGREED

counsels, that the facts hereinafter stated shall be taken as true, provided, however, that this stipulation shall be without prejudice to the right of either party to introduce upon the trial of this case any other and further evidence not inconsistent with the facts herein stipulated:

1.

Plaintiff brings this action against defendant pursuant to Section 1346(a)(1) of Title 28 of the United States Code, Act of June 25, 1948, c. 646, 62 Stat. 869, 933, as amended by the Act of May 24, 1949, c. 139, Par. 80(a), 63 Stat. 89, 101, as amended by the Act of July 30, 1954, c. 648, 1, 68 Stat. 589.

2.

This action is brought by Reliance Clay Products Company for the recovery of:

(a) $22,944.20 of income tax and interest thereon as provided by law for the calendar year 1951; and

(b) $3,228.61 of income tax and interest thereon as provided by law for the calendar year 1952.

3.

Plaintiff is a corporation incorporated and doing

principal place of business at Dallas, Dallas County, Texas, within this District and Division.

4.

Plaintiff keeps its books and reports for Federal Income Tax returns, on the accrual basis method of accounting, on a calendar year basis.

5.

Within the time prescribed by law, plaintiff made and filed its income tax returns for the calendar years 1951 and 1952, showing an income tax liability of $37,389.60 for 1951 and of $4,735.55 for 1952, and no excess profits tax liability for either year.

6.

The income tax liabilities shown on such returns were paid on or about the following dates:

(a) Calendar year 1951 Return:

13,086.36 on March 1, 1952
24,303.24 on June 8, 1952
37,389.60

(b) Calendar year 1952 Return:

1,895.55 on March 14, 1953
1,420.00 on June 13, 1953
1,420.00 on August 11, 1953
1,735.55

Checks in payment were presented on or before the due dates required by law.

7.

The Commissioner of Internal Revenue, hereinafter sometimes referred to as the Commissioner, caused the aforesaid income tax returns of plaintiff for 1951 and 1952 to be examined and Revenue Agent's Reports to be submitted as follows:

(a) For 1951 the Revenue Agents' Report dated February 2, 1953, stating the result of such examination was transmitted to plaintiff under date of February 18, 1953, by Ellis Campbell, Jr., District Director of Internal Revenue in Dallas, Texas. Such report allowed plaintiff a deduction for percentage depletion computed as stated in paragraph 13 *infra*.

(b) For 1952, the Revenue Agents' Report dated October 28, 1954 stating the result of such examina-

of Internal Revenue in Dallas, Texas. Such report allowed plaintiff a deduction for percentage depletion computed as stated in paragraph 13 *infra*.

8.

The Revenue Agents' Reports referred to in paragraph 7, supra, proposed deficiencies in income taxes as follows:

(a) For 1951, of $46,994.96 on the basis that the deduction for percentage depletion and the deduction for depreciation which plaintiff had taken on its return was excessive.

(b) For 1952, of $3,228.61 on the basis that the deduction for percentage depletion which plaintiff had taken on its return was excessive.

9.

(a) Pursuant to such Revenue Agents' Report for 1951, the Commissioner made an additional assessment of $9,652.89 of income tax and of $562.64 of interest thereon representing additional amounts due on the depreciation adjustment referred to in paragraph 8, supra, which $10,215.53 was received by the Commissioner on March 20, 1953 (account #529000). Subsequent thereto, and pursuant to such Revenue Agents' Report, the Commissioner made an additional

$8,619.47 of excess profits taxes) and of $5,233.94 of interest thereon, which was received by the Commissioner on July 16, 1954 and August 6, 1954, respectively (account #528906).

(b) Of the original refund claim of $37,341.47, $8,619.47 was refunded by the Government, this being the excess profits tax paid which it was determined was erroneously calculated and it was agreed by the tax payer that $5,777.80 should be eliminated since this item was based on transportation costs not subject to depletion, leaving the total amount of disallowed depletion claimed in this suit of $22,944.20, together with interest as provided by law.

(c) Pursuant to such Revenue Agent's Report for 1952, the Commissioner made an additional assessment of $3,228.61 of income tax and of $329.76 of interest thereon representing additional amounts due on the depletion adjustment referred to in paragraph 8, *supra*, which total of $3,558.27 was collected by the Commissioner through a credit against an overassessment of $8,619.47 representing excess profits taxes refunded as a result of the Revenue Agents' Examination for 1952 referred to in paragraph 7, *supra*. (Reference Schedule No. IT:B-1849, with no date.)

10.

On July 27, 1955, plaintiff duly filed with the Dis-

trict of Texas at Dallas, Texas a claim for refund of income taxes for 1951, and also a claim for refund of income taxes for 1952. These two separate claims represented the additional amounts paid for the adjustments to depletion pursuant to such additional assessments referred to in paragraph 9, *supra*.

Such claims for refund alleged that plaintiff is entitled to a percentage depletion deduction on its deposits of brick and tile clay, computed on the selling price, f.o.b. plant, loaded for shipment, of the burnt brick and tile which it produces. Such deductions are greater than those allowed by the Revenue Agents' Reports referred to in paragraph 7, supra. Such claims for refund set forth the grounds and reasons upon which this suit is brought. True and correct photostatic copies of the claims for refund for 1951 and 1952 were attached to the original complaint in this cause and marked as Exhibits A and B respectively.

11.

On January 13, 1946 Ellis Campbell, Jr., the District Director of Internal Revenue, Dallas, Texas under Section 3772(a)(2) of the Internal Revenue Code of 1939 (Sec. 6532(a)(1) of the Code of 1954) mailed by registered mail separate notices of disallowance of the 1951 and 1952 claims for refund of income taxes filed on July 27, 1955. True and correct copies of such notices of disallowance were attached to the

original complaint in this cause and marked as Exhibits C and D. The claims for refund were disallowed on the ground that the amounts of the deductions for percentage depletion which plaintiff was claiming was excessive and that plaintiff therefore had not overpaid its taxes.

12.

It is agreed that if plaintiff is entitled to a deduction for depletion on its gross income from mining as computed by the Internal Revenue Agent and as alleged in paragraph 13, *infra*, the accounting method and the depletion deductions as computed pursuant thereto for the calendar years 1951 and 1952 are correct. If plaintiff has overpaid its income taxes based on plaintiff's method of computation of gross income from mining, based on 5 per cent of the sales price of its brick and tile clay, f.o.b. plant, loaded for shipment, the plaintiff has overpaid its income taxes in the amount of $22,944.20 for 1951 and in the amount of $3,228.61 for 1952.

13.

The deductions which the Commissioner allowed plaintiff for percentage depletion in accordance with the Revenue Agents' Reports referred to in paragraph 7 *supra*, were as follows:

(a) For 1951, the Revenue Agent arrived at a

plaintiff's income tax return were classified in three ways: (1) Manufacturing, (2) Selling, and (3) Administrative.

The Agents' Report allocated profits earned to (1) Mining costs; (2) Manufacturing costs and (3) Selling costs, but no allocation of profits to (4) Administrative costs. The administrative costs were then allocated to the other three classifications in accordance with the percentage of costs of each, without the administrative costs, as follows:

	Direct Total Amount	%	Administrative	Total
Mining	78,842.90	7.70	4,186.43	83,029.33
Manufacturing	612,802.89	59.83	32,529.08	645,331.97
Selling	332,557.55	32.47	17,653.67	350,211.22
	1,024,203.34	100.00	54,369.18	1,078,572.52

To the manufacturing expenses was then added the opening inventory of $21,383,36 and the year end and closing inventory of $43,860.74 was deducted. Based on total costs, the Revenue Agents' Report allocated, as stated above, to mining, manufacturing and selling the profits of the company as follows:

	Adjusted Total Cost Amount		Profits Allocated	Total
Mining	83,629.33	7.86	13,554.06	96,583.39
Manufacturing	622,854.59	58.98	101,707.22	724,561.81
Selling	350,211.32	33.16	57,182.28	407,393.50
	1,056,695.24	100.00	172,443.56	1,228,538.70
Difference not located by Revenue Agent				53.74
Total Sales				1,228,484.96

The Revenue Agents' Report then applied the five per cent (5%) depletion allowance to $96,583.39 termed "gross income from mining" for a total depletion deduction of $4,829.17.

(b) For 1952, the Revenue Agent also arrived at a cost figure termed "mining." All other costs of the plaintiff's income tax return were classified as: (1) manufacturing expense, (2) handling expense (3) selling expense, (4) other expense, and (5) administrative expense.

After allocation of the Administrative expense and adjustment for opening and closing inventories as outlined in paragraph 13(a), *supra*, the Revenue Agents' Report allocated to each operation the profit of the company as follows:

	Adjusted Amount	Total Cost	Profits Allocated	Total
Mining	110,302.93	10.30	3,251.75	113,554.6
Manufacturing	427,221.86	39.90	12,596.57	439,818.4
Handling	147,995.96	13.74	4,337.76	151,433.7
Selling	383,340.11	35.80	11,302.18	394,642.2
Other	2,896.98	.26	82.68	2,889.0
	1,070,767.84	100.00	31,570.34	
Gross Sales				1,102,338.1

The Revenue Agents' Report then applied the fiv per cent (5%) depletion allowance to 113,554.68 termed "gross income from mining" for a total deple tion deduction of $5,677.73.

14.

Exhibit A, Exhibit B, Exhibit C and Exhibit D each attached to the original complaint filed herei are true and correct photostatic copies of the docu ments they purport to be, and it is agreed that eac may be placed in evidence without further proof o execution.

15.

It is agreed that the following processes are applie by plaintiff to the mineral product clay in order t manufacture burnt brick or tile which are sold by th plaintiff:

(a) The clay is mined by a drag line and loaded in dump trucks which carry the clay to a nearby plant.

(b) The clay taken to the plant is sometimes weathered in a storage shed.

(c) The clay is either dumped directly from the dump truck or is taken from the storage shed and placed in a feeder from which the clay passes into a dry pan crusher, which crushes and grinds the clay.

(d) The clay is discharged from the dry pan crusher onto the elevator belt which carries it to a screen.

(e) The clay passes through the screen into a bin; from the bin the clay passes into a feeder.

(f) The clay is discharged from the feeder into the pug mill, which is a machine wherein water is added as the final tempering process.

(g) From the pug mill the clay passes into the brick or tile machine. It first goes into an evacuation chamber where air is evacuated from the clay by a vacuum pump. The clay then passes into the extrusion section of the machine where it is forced under pressure through various types of dies in long ribbons.

(h) The long ribbons of clay as extruded through the dies pass into the cutting machine which cuts them into clay units of desired size.

(i) The clay units as cut pass onto a conveyor be and are then stacked onto dryer or kiln cars which a moved to the dryer tunnels or to the continuous tu nel-kiln, where free water is evaporated from the cl units by open gas fires, or waste heat from kiln.

(j) When the free water is thus removed the cl units are either stacked in periodic kilns, or in t case of continuous or tunnel-kilns are left on the ki cars which continue from the dryer to the kiln.

(k) The clay units are then burned by natur gas fires whether in periodic or continuous (tunne kilns.

(l) The burnt brick and tile is then removed fro the kilns.

(m) After it has been removed from the kilns t burnt brick and tile is either stacked on the yard o loaded directly for shipment to purchasers.

16.

Of the above processes the Commissioner has in cluded in the computation of gross income from mi ing as applied by plaintiff to the mineral product cl in order to manufacture burnt brick and tile, the fo lowing:

A. Costs of extraction:

(a) Dragline operation by which the clay is extracted from the pit.

(b) Loading of the bulk clay in dump trucks which carry the clay to a nearby plant.

B. Costs of treatment:

(a) Dumping of the trucks loaded with clay into the storage shed where the clay is weathered.

(b) Placing the clay into a feeder from which the clay passes into a crusher.

(c) The dry pan crusher which crushes and grinds the clay.

(d) The clay is discharged from the dry pan crusher onto an elevator belt which carries it to a screen, from whence it passes through the screen to a storage bin.

17.

The following processes the Commissioner has not included in the computation of gross income from mining. It is the Government's contention that all processes applied to the mineral product clay in this paragraph are not mining treatment processes but manufacturing processes by which the clay is changed

from the form in which it emerged from the min
It is the taxpayer's contention that all of the process
in this paragraph are ordinary treatment process
within the meaning of Section 114(b)(4)(B) of th
Internal Revenue Code of 1939.

(a) The clay which has been screened is picke
up by the feeder and discharged into the pug mil
which is a machine wherein water is added as a fin
tempering process.

(b) From the pug mill the clay passes into th
brick or tile machine. It first goes into an evacuatio
chamber where air is evacuated from the clay by
vacuum pump. The clay then passes into the extru
sion section of the machine where it is forced unde
pressure through various types of dies in long ribbon

(c) The long ribbons of clay as extruded throug
the dies pass into the cutting machine which cuts the
into clay units of desired size.

(d) The clay units as cut pass onto a conveyo
belt and are then stacked onto dryer or kiln cars whic
are moved to the dryer tunnels or to the continuou
tunnel-kiln, where free water is evaporated from th
clay units by open gas fires, or waste heat from kil

(e) When the free water is thus removed the cla
units are either stacked in periodic kilns or in th
case of continuous or tunnel-kilns are left on the kil

(f) The clay units are then burned by natural gas fires whether in periodic or continuous tunnel-kilns.

(g) The burnt brick and tile is then removed from the kilns.

(h) After it has been removed from the kilns, the burnt brick and tile is either stacked on the yard or loaded directly for shipment to purchasers.

18.

There is no clay which by its physical or chemical characteristics can be identified as being only brick and tile clay. The term "brick and tile clay" as used in Section 114(b)(4)(A) of the Internal Revenue Code is defined by Section 29.23(n)-5 of Treasury Regulations 111, as amended, by Treasury Decision 6031, approved July 14, 1953, as follows: "Clay used or sold for use in the manufacture of common brick, drain, and roofing tile, sewer pipe, flower pots, and kindred products (other than clay specifically identified as a clay for which a 15 per cent rate of percentage allowance is provided)."

19.

The parties hereto stipulate and agree that if this Honorable Court grants to the plaintiff the relief sought by the plaintiff, the plaintiff is entitled to a judgment for refund as follows:

(a) $22,944.20 for the calendar year 1951; and

(b) $3,228.61 for the calendar year 1952, with

(c) Interest on each amount, as provided by law.

20

That all prerequisites to the filing of this suit by the taxpayer have been taken and complied with.

Respectfully Submitted,

TURNER, RODGERS, WINN SCURLOCK & TERRY

By /s/ George S. Terry
2400 Republic National Bank Building
Dallas, Texas

ATTORNEYS FOR PLAINTIFF

/s/ John C. Ford
JOHN C. FORD, ASSISTANT UNITED STATES ATTORNEY

ATTORNEY FOR DEFENDANT, UNITED STATES OF AMERICA

STIPULATION OF FACTS NO. 2

The parties hereto by their respective attorneys hereby stipulate and agree that upon the trial of the above case, the following facts shall be taken as true, subject, however, to the right of either party to object to the relevancy of any fact stated herein, and further subject to the right of either party to introduce other and further evidence not inconsistent with any of the facts stated herein.

INTRODUCTION

1. Part I of this stipulation summarizes the results of a nationwide sales survey conducted by the defendant herein, through the Internal Revenue Service, to determine the amount of clay sold for use in the production of brick, tile, and kindred products. The Washington office of the Internal Revenue Service instructed every District Director in the United States to ascertain the facts as to any sales of clay for such purposes in each District. The results of this survey were communicated to, and checked by, the plaintiff. The facts stipulated in Parts I and II herein as to sales of clay in the years 1951 to 1955 are as shown by the survey conducted by defendant and as supplemented by information obtained through affidavits by plaintiff. Part I of this stipulation is a chart which shows the sales referred to above, giving the name of the seller, the name of the purchaser, year of sale, tons sold, price per ton, total amount, product,

and pyrometric cone equivalent (p.c.e.) where this is known.

2. Part II of this stipulation contains further facts concerning the sales referred to in Part I hereof. This information is classified by purchaser. For convenience, all sales to each purchaser are repeated under the name of that purchaser.

3. Part III of this stipulation contains figures prepared by the Bureau of Mines as to the amount of "miscellaneous clay" sold to make "heavy clay products." "Heavy clay products" include building brick and tile, paving brick, drain tile, sewer pipe, and kindred products.

a. The Bureau of Mines of the United States Department of the Interior annually collects, and publishes in the Minerals Yearbook, information concerning the production, use, and sale of the various types of clays and other minerals mined in the United States.

b. This information is obtained from questionnaires distributed to producers (i.e., miners) of minerals. A copy of the questionnaire used is attached hereto as Exhibit A of Part III. Each producer fills in such questionnaire and returns it to the Bureau of Mines. No information is obtained from the purchasers of minerals who are not also producers. The information concerning the use of a mineral sold is obtained only from the producer of such mineral.

c. When the Bureau of Mines receives such questionnaires, they are checked for errors and inconsistencies apparent on their face by the Ceramics and Fertilizer Materials Branch of the Bureau of Mines. If any such errors or inconsistencies are found, the Bureau of Mines asks the producer supplying the information to correct such items. No further check of the information received is made at the source.

d. From these questionnaires, the Ceramics and Fertilizer Materials Branch prepares certain tables for publication in the Minerals Yearbook. One such table shows the tons of clay sold or used by producers, classified by kinds of clay and uses of such clay. True and correct copies of such tables for 1951 through 1953 are attached hereto as Exhibits B, C, and D of Part III. A separate table is prepared for each year to show the tons of "miscellaneous clay" sold and used by producers, and the value thereof. True and correct copies of such tables for 1951 to 1953 are attached hereto as Exhibits E and F of Part III. This information has not, as yet been compiled for any year subsequent to 1953.

e. The Bureau of Mines does not publish any figures showing the quantity of miscellaneous clay sold for use in making heavy clay products because it is not considered worth the effort to edit and compile them separately.

f. At the request of the Department of Justice,

cellaneous clay sold by producers for use in making heavy clay products as shown by the questionnaires received from producers. Transfers among different plants controlled by one group known to be such by the Bureau of Mines, were eliminated. The results of this computation are set forth herein as Part III of this stipulation.

g. The questionnaires received from producers are confidential and the contents of individual questionnaires cannot be divulged. Therefore, the parties have not been able to check the accuracy of the figures. Because of the confidential nature of the questionnaires, figures for one state cannot be divulged unless at least three producers in that state sell miscellaneous clay for heavy clay products. The Bureau of Mines cannot give any more of a breakdown to show where the sales occurred than appears in lines 17 to 23 of the chart in Part III.

h. The amount of miscellaneous clay shown on this chart as sold for heavy clay products is the outside limit on the amount sold for this purpose and the parties stipulate that no more than this amount is sold for such purposes than is shown on such chart. The parties do not stipulate further as to the accuracy of such figures, but they do stipulate that the figures were compiled in the manner and from the sources set forth above.

4. The Bureau of Census of the United States De-

the manufacturing companies in the United States. The census shows that in 1947 there was a total of 674 establishments producing "Brick and Hollow Tile." A true and correct copy of the table showing this information as published by the Bureau of the Census is attached hereto as Exhibit G. The Structural Clay Products Institute of Washington, D.C., a trade association of producers of structural clay products, compiles a directory of the structural clay products industry. Such directory has contained a listing of the following number of companies at the times indicated:

Date	No. of Companies
June, 1949	641
November, 1953	579
April, 1955	563
March, 1956	566

5. The clay shown as sold by Maumee Collieries Company and by Lincoln Clay Products Company, in Parts I and II of this stipulation, for use in making structural brick and other non-refractory products, has also been sold for making refractory brick and other refractory products.

	1951	1952	1
Forest Tons Sold	252,496.66	298,949.25	10
Total Value	$465,629.82	$631,356.38	$76

Year	P.C.E. Under 15	P.C.E. 15-18	P. 19 and
1951	105,152	24,570	123,7
1952	82,283	11,301	203,1
1953	105,228	15,590	273,9
1954	126,546	10,311	304,0
1955	131,724	52,281	324,7
Totals	550,933	111,053	1,229,8

53	1954	1955
,646.92	445,178.43	512,358.50
,996.25	$673,753.39	$1,016,133.62

.E. Over	P.C.E. Unknown	Total
74.66	2,000	252,496.66
49.25	2,216	298,949.25
54.92	7,874	402,646.92
26.43	1,295	445,178.43
03.60	3,379.9	512,358.50
78.86	19,761.9	1,911,629.76

Seller
Sunset Brick & Tile Co.
(Snyder, Texas)

Year	Tons	Price Per Ton	Amount
1954	78.00	$ .77	$ 60.00
1955	520.00	.77	400.40
	598.00		$ 460.40

CALIFOR

Seller
Lincoln Clay Products Co.
(Lincoln, Calif.)

1951	6,582.00	$1.50	$ 9,873.00
1952	5,228.00	1.50	7,842.00
1953	4,660.00	1.75	8,155.00

Buyer Southwestern Brick & Tile Co. (Snyder, Texas)	
Product	**Pyrometric Cone Equiv.**
Brick	Under 15
Brick	Under 15

NIA

Buyer Craycroft Brick Co. (Fresno, Calif.)	
Drain, roofing tile, common, face brick structural tile	30-32
Drain, roofing tile, common, face brick structural tile	30-32
Drain, roofing tile, common, face brick structural tile	30-32

1954	3,893.00	1.75	6,813.00
1955	4,212.00	1.75	7,371.00
	24,575.00		$ 40,054.00

Seller
Remillard-Dandini
(Calif.) (Parent)

1951*	36,930.00	.87	32,129.00
1952	46,641.00	.92	42,910.00
1953	49,714.00	.90	44,743.00
1954	38,079.00	.63	23,990.00
1955	29,764.00	.89	26,490.00
	201,128.00		$170,262.00

*All years are fiscal years ending May 31

Drain, roofing tile, common, face brick structural tile	30-32
Drain, roofing tile, common, face brick structural tile	30-32

Buyer

San Jose Brick & Tile Co.
(San Jose, Calif.)
(Subsidiary)

Brick and tile	Under 15
Brick and tile	Under 15
Brick and tile	Under 15
Brick and tile	Under 15
Brick and tile	Under 15

PART II.

I. L. STILES & SON BRICK COMPANY
(North Haven, Connecticut)

Purchases of Clay
Use: Common Brick

Year	Tons	Price per ton	Seller
1953	25,000	$ .66	North Haven Brick Co.
1954	61,608	.75	North Haven Brick Co.
1955	61,981	.75	North Haven Brick Co.

I. L. Stiles & Son Brick Company, the buyer, owns 137 shares of the outstanding 150 shares of stock of the North Haven Brick Company, the seller. Of the remaining 13 shares of the stock of the North Haven Brick Company, 12 are owned by the principal stockholder of I. L. Stiles & Son Brick Company and members of his family.

The parent company has its own clay pit, but has used the subsidiary company's clay in these years for the following reasons:

1. The clay of the subsidiary produces a superior brick.

2. It is cheaper to operate only one pit.

3. The overburden (top soil, etc.) of the property from which the subsidiary's clay is mined is used to make other products in a plant adjacent to the subsidiary's clay pits, and the management desired to provide the maximum quantity possible of overburden for such plant.

The price per ton is based on the expenses incurred by the subsidiary company in mining the clay, and is intended to repay the subsidiary for such costs.

This clay obtained from North Haven Brick Company has a pyrometric cone equivalent under 15.

	Tons of Denver Terra Cotta Company's own Clay Used for Architectural Terra Cotta
1951	420
1952	290
1953	305
1954	175
1955	481

This company purchases clay because its own clay contains silica sand. It is necessary to mix a plastic clay with such clay in order to make a body of clay suitable for the terra cotta produced. The clay purchased burns a buff color.

The clay purchased from Big Bend Collieries, Inc., has a pyrometric cone equivalent of 27. The parties

have verified the pyrometric cone equivalent of the clay purchased from Big Bend Collieries.

The parties do not know the pyrometric cone equivalent of the clay purchased from Cedar Heights Clay Company.

COLORADO-MISCELLANEOUS PURCHASERS

Various brick companies in Colorado buy a total of approximately 2,000 tons per year of clay. The amounts purchased by each company are small. The parties do not know what products are made from this clay, and they do not know what type of clay this is.

SOUTHWESTERN BRICK & TILE COMPANY

(Snyder, Texas)

Purchases of Clay
Use: Brick

Year	Tons	Price per ton	Seller
1954	78	$ .77	Sunset Brick & Tile Company
1955	520	.77	Sunset Brick & Tile Company

This company's own clay burns a deep red, and the purchased clay burns a buff color. Southwestern purchases clay to mix it with its own clay in order to make

Sunset Brick & Tile Co., makes no profit on this sale of clay; the price was fixed so as to pay Sunset its cost of mining the clay. Sunset sells the clay because the president of Sunset is a close personal friend of the owner of Southwestern and because Sunset wants to obtain production data on the use of its clay in the stiff mud process of making brick used by Southwestern (Sunset uses a dry press method).

The clay purchased has a pyrometric cone equivalent of under 15.

CRAYCROFT BRICK COMPANY
(Fresno, California)

Purchases of Clay

Use: Drain and Roofing Tile, Sewer Pipe, Common Brick, Face Brick, Structural Tile and Kindred Products

Year	Tons	Price per ton	Seller
1951	6,582	$1.50	Lincoln Clay Products Company
1952	5,228	1.50	Lincoln Clay Products Company
1953	4,660	1.75	Lincoln Clay Products Company
1954	3,893	1.75	Lincoln Clay Products Company

Tons of Craycroft Brick Company's Own Clay Used for Clay Products

1951	15,280
1952	14,461
1953	14,410
1954	17,712
1955	22,140

The purchased clay is mixed with Craycroft's own clay in the production of the clay products listed above. Craycroft's own clay does not have sufficient plasticity to make a satisfactory quality brick, and another clay has to be mixed with the company's own clay in order to make a brick with sufficient strength to meet A.S.T.M. standards on government, state, and county specifications. The purchased clay is a plastic clay and compensates for the lack of plasticity in Craycroft's own clay.

A. Miscellaneous Clay Sold and Used for Various Purposes	1951 Short Tons	1951 Dollar Value
1. Tons sold by producer for use in heavy clay products (Specially prepared by Bureau of Mines from questionnaires)	84,402	$ 104,555
2. Total tons sold by producer for all purposes (Minerals Yearbook)	989,739	2,025,912
3. Tons sold by producer for use in making cement (Minerals Yearbook)	658,450	660,936
4. Tons sold by producer for purposes other than heavy clay products and cement (Line 2 minus Line 1 minus Line 3)	247,000	1,260,000
5. Total tons sold or used by producer for heavy clay products (Minerals Yearbook)	19,126,414	
6. Total tons sold or used by producer for all purposes (Minerals Yearbook)	27,649,491	29,692,830
B. Percentages based on Above Figures		
7. Percentage of miscellaneous clay mined which is sold by producers for heavy clay products (Line 1 divided by Line 6)		
8. Percentage of all clay sold or used by producers for heavy clay products which is sold by producers (Line 1 divided by Line 5)		
9. Percentage of all clay sold by producers which is sold for heavy clay products by producers (Line 1 divided by Line 2)		

1952		1953	
Short Tons	Dollar Value	Short Tons	Dollar Value
230,295	$ 252,895	342,506	$ 554,614
1,604,851	3,713,415	1,504,946	2,872,664
790,531	813,301	734,706	733,725
584,000	2,647,000	427,000	1,594,000
17,587,646		18,243,673	
26,907,910	31,179,891	28,278,307	32,424,198

1951 Percentage	1952 Percentage	1953 Percentage
.30	.85	1.21
.44	1.31	1.88
8.53	14.3	22.8

C. Average Value Per Ton of Miscellaneous Clay (Total Value Divided by Tons)	1951	1952	1953
10. Sold by producers for heavy clay products (Line 1)	$ 1.24	$ 1.10	$ 1.62
11. Total sold or used by producers for all purposes (Line 6)	1.07	1.16	1.15
12. Sold by producers for use in making cement (Line 3)	1.00	1.03	1.00
13. Used by producers in making cement (Minerals Yearbook)	1.02	1.00	.98
14. Sold by producers for purposes other than heavy clay products and cement (Line 4)	5.10	4.53	3.73
15. Sold by producers for all purposes (Line 2)	2.05	2.31	1.91
16. Used by producers for all purposes (Minerals Yearbook)	1.04	1.10	1.10

D. Breakdown by States of Miscellaneous Clay W
Clay Products (Specially prepared by Bureau

	1951 Short Tons-Doll
17. Ohio and New York	38,916
18. Colorado	C
19. California	C
20. Indiana and Illinois	C
21. Iowa, Minnesota & Missouri	C
22. New Jersey, Pennsylvania and North Carolina.	C
23. Other states which include Colorado, Indiana, California, Oklahoma, Montana, Texas, Pennsylvania, Washington, North Dakota, & Wisconsin	45,486

"C" means combined with "Other States" in o
disclosure of individual firm's data.

...ich Was Sold by Producer for Use in Heavy
...of Mines from questionnaires)

	1952		1953	
...r Value	Short Tons	Dollar Value	Short Tons	Dollar Value
...59,069	123,556	$135,862	156,737	$236,447
	(No. N.Y.)			
C	21,267	43,415	47,278	81,900
	C	C	6,639	5,417
C	21,914	22,156	108,233	199,386
C	28,367	31,257	1,564	3,177
	(No. Missouri)			
C	C	C	18,782	16,972
...15,486	35,251	20,205	3,273	11,315

...der to avoid

IN WITNESS WHEREOF, this stipulation, consisting of 42 pages and Exhibits A through G, has been duly signed by the attorney for plaintiff and the attorney for defendant this 12th day of May, 1956.

s George S. Terry
ATTORNEY FOR PLAINTIFF

s John C. Ford
Assistant U. S. Attorney

ATTORNEY FOR DEFENDANT,
UNITED STATES OF AMERICA

NOTICE OF APPEAL

Filed July 11, 1956

NOW COMES the United States of America, defendant, by and through its attorney of record herein, Heard L. Floore, United States Attorney for the Northern District of Texas, and hereby gives notice of appeal to the United States Court of Appeals for the Fifth Circuit from the final judgment rendered on May 12, 1956, and entered herein on May 15, 1956.

s/ Heard L. Floore
Heard L. Floore
United States Attorney

s/ John C. Ford
John C. Ford, Assistant
United States Attorney

Attorneys for Appellant

CERTIFICATE OF SERVICE

I hereby certify that on Wednesday, July 11, 1956, I served a copy of the foregoing notice of appeal on Mr. George S. Terry of Turner, Rodgers, Winn, Scurlock & Terry, attorneys for plaintiff, by depositing one copy thereof in the United States mail in a Government-franked envelope, requiring no postage, addressed to said attorney at 2100 Republic National Bank Building, Dallas, Texas, which address is the last address of the said attorney known to me.

s/ John C. Ford
John C. Ford, Assistant
United States Attorney

ORDER GRANTING EXTENSION OF TIME

On motion of the appellant the United States of America, in the above entitled and numbered cause, by and through its attorney of record, Heard L. Floore, United States Attorney for the Northern District of Texas, and the Court being fully advised, it is

ORDERED that the time for filing the record on appeal in the United States Court of Appeals for the Fifth Circuit and the docketing therein of the appeal taken by the appellant, United States of America, by notice of appeal filed on the 11th day of July, 1956, be and is hereby extended to October 9, 1956, pursuant to Rule 73(g) of the Federal Rules of Civil Procedure. Aug. 9, 1956.

/s/ Wm. H. Atwell
UNITED STATES DISTRICT JUDGE

DESIGNATION OF RECORD ON APPEAL

Pursuant to Rule 75(a) of the Federal Rules of Civil Procedure, the defendant-appellee herein, United States of America, by its attorney, Heard L. Floore, United States Attorney for the Northern District of Texas, hereby designates for inclusion in the record on appeal to the United States Court of Appeals for the Fifth Circuit, taken by notice of appeal filed in this cause on the 11th day of July, 1956, the following portions of the record, proceedings, and evidence in this cause, to-wit:

1. Original complaint

2. Original answer

3. Transcript of proceedings (which includes findings of fact, conclusions of law, and Court's oral opinion.)

4. Judgment

5. Plaintiff's Exhibit No. 1

6. Plaintiff's Exhibit No. 2

7. Notice of appeal

8. Order granting extension of time for filing and docketing record on appeal

9. This designation.

s/ Heard L. Floore
Heard L. Floore
United States Attorney

s/ John C. Ford
John C. Ford, Assistant
United States Attorney

CERTIFICATE OF SERVICE

I hereby certify that on Thursday, October 4, 1956, I served a copy of the foregoing designation of record on appeal on the Honorable George S. Terry, attorney for the plaintiff-appellee herein, by depositing one copy thereof in the United States mail in a Government-

franked envelope requiring no postage addressed to said attorney at 2400 Republic National Bank Building, Dallas, Texas, which address is the last address of the attorney known to me.

s John C. Ford
John C. Ford, Assistant
United States Attorney

CLERK'S CERTIFICATE

I, George W. Parker, Clerk of the United States District Court for the Northern District of Texas, do hereby certify that the foregoing is a true and correct transcript of the record and all proceedings in cause Number 6400 Civil, wherein Reliance Clay Products Company is plaintiff and The United States of America is defendant, as fully as the same now remain on file and of record in my office at Dallas, Texas.

WITNESS my hand officially and the seal of said Court at Dallas, Texas, this the 4th day of October A.D. 1956.

George W. Parker, Clerk
U. S. District Court
Northern District of Texas

By /s/ Mary Conger
Chief Deputy Clerk

FILED
JUN 24 1957
JOHN T. FEY, Clerk.

No. 1120

In the Supreme Court of the United States

OCTOBER TERM, 1956

UNITED STATES OF AMERICA, ET AL., PETITIONERS

v.

ERRY BROTHERS BRICK AND TILE COMPANY, ET AL.

TITION FOR A WRIT OF CERTIORARI TO THE UNITED TATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

HERBERT BROWNELL, JR.,
Attorney General,
JOHN N. STULL,
Acting Assistant Attorney General,
HARRY BAUM,
SHELDON I. FINK,
Attorneys,
Department of Justice,
Washington 25, D. C.

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CITATIONS

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Internal Revenue Code of 1939:

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Sec. 23(n) (26 U.S.C. 1952 ed., Sec. 23(n)) 8, 41

Sec. 114(b) (26 U.S.C. 1952 ed., Sec. 114(b)), 8, 9, 12, 16, 20, 21, 41

Internal Revenue Code of 1954:

Sec. 611(a) (26 U.S.C. 1952 ed., Supp. II, Sec. 611(a)) 12, 44

Sec. 613(a) (26 U.S.C. 1952 ed., Supp. II, Sec. 613(a)) 45

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Revenue Act of 1926, c. 27, 44 Stat. 9, Sec. 204(c) 15

Revenue Act of 1932, c. 209, 47 Stat. 169:

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Revenue Act of 1943, c. 63, 58 Stat. 21:

Sec. 124(c) (26 U.S.C. 1952 ed., Sec. 114(B)) 16

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Revenue Act of 1951, c. 521, 65 Stat. 452, Sec. 319 (26 U.S.C. 1952 ed., Sec. 114(b)) 9, 17

Miscellaneous:

1 House Hearings Before Committee on Ways & Means, 77th Cong., 2d Sess., Revenue Revision of 1942, pp. 1199-1202 16

Minerals Yearbook, 1951, United States Department of Interior, Bureau of Mines, pp. 293-295 21

S. Rep. No. 627, 78th Cong., 1st Sess., pp. 23-24 (1944 Cum. Bull. 973, 992 17

S. Rep. No. 2375, 81st Cong., 2d Sess., p. 53 (1950-2 Cum. Bull. 483, 522 17

Senate Hearings before the Committee on Finance, 78th Cong., 1st Sess., on Revenue Act of 1943, pp. 527-529. 16

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In the Supreme Court of the United States

OCTOBER TERM, 1956

No. —

UNITED STATES OF AMERICA, ET AL., PETITIONERS

v.

MERRY BROTHERS BRICK AND TILE COMPANY, ET AL.[1]

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

The Attorney General,[2] on behalf of petitioners, prays that a writ of certiorari issue to review the judgments of the United States Court of Appeals for the Fifth Circuit in the above-entitled cases.

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[1] Pursuant to Rule 23(5) of the Revised Rules of this Court, this petition for a writ of certiorari covers thirteen cases decided by the United States Court of Appeals for the Fifth Circuit. Although separate judgments were entered, all thirteen cases involve substantially identical questions. The cases (other than the title case) are: *United States of America* v. *Reliance Clay Products Co.*; *United States of America* v. *Estate of L. L. Stephenson, the First National Bank of Birmingham as Executor, et al.*; *United States of America* v. *Tupelo Brick & Tile Co.*; *United States of America* v. *Elgin-Butler Brick Co.*; *Paul Cobb, District Director of Internal Revenue* v. *Chattahoochie Brick Co.*; *United States of America* v. *Atlanta Brick & Tile Co.*; *United States of America* v. *Acme Brick Co.*; *Ellis Campbell, District Director of Internal Revenue Service and United States of America* v. *Carney Kirby and wife, Geneva Kirby, et. al.*; *United States of America* v. *Teague Brick & Tile Co.*; *United States of America* v. *Cherokee Brick & Tile Co.*; *United States of America* v. *Burns Brick Co.*; *United States of America* v. *Texas Vitrified Pipe Co.*

[2] For personal reasons, the Solicitor General has disqualified himself from participating in this litigation.

OPINIONS BELOW

The opinion of the District Court in *United States v. Merry Brothers Brick and Tile Co.* is reported at 145 F. Supp. 186. (R. 54-63.) The District Court did not file an opinion in *United States v. Reliance Clay Products Co.* The opinion of the Court of Appeals in these two cases (Appendix A, *infra*, pp. 23-30) is reported at 242 F. 2d 708. No opinions were written in the remaining companion cases.[3]

JURISDICTION

The judgments of the Court of Appeals in *United States v. Merry Brothers Brick and Tile Co.*, and *United States v. Reliance Clay Products Co.* were entered on March 27, 1957. (Appendix A, *infra*, pp. 23, 30.) Judgments of the Court of Appeals in the remaining cases were entered on April 25, 1957, with the exception of *United States v. Teague Brick & Tile Co.* (entered April 29, 1957), *United States v. Cherokee Brick & Tile Co.* and *United States v. Burns Brick Co.* (entered May 3, 1957), and *United States v. Texas Vitrified Pipe Co.* (entered May 10, 1957). (Appendix A, *infra*, pp. 30-40.) The jurisdiction of this Court is invoked under 28 U.S.C., Section 1254.

QUESTION PRESENTED

Whether "gross income from mining", on the basis of which percentage depletion for mineral deposits is allowable under Sections 23(m) and (n), and 114(b)(4) of the Internal Revenue Code of 1939, includes income derived from manufacturing merely because the

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[3] The *Merry Brothers* and *Reliance Clay* cases were heard and decided together by the court below. In the other cases, it was stipulated that judgments would be entered by that court in conformity with the decision in those cases.

mine owner, in addition to engaging in mining activities, transforms the mineral into a manufactured product and sells it as such.

The answer depends on whether the mine owner's manufacturing operations are to be considered "ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product", within the meaning of Section 114(b)(4)(B).

STATUTES AND REGULATIONS INVOLVED

The pertinent provisions of Sections 23(m) and (n) and 114(b)(4) of the Internal Revenue Code of 1939, Sections 611(a) and 613(a), (b) and (c) of the Internal Revenue Code of 1954, Section 29.23(m)-1 of Treasury Regulations 111, and of Section 39.23(m)-1 of Treasury Regulations 118, are set forth in Appendix B, *infra*, pp. 41-56.

STATEMENT

Merry Brothers Brick and Tile Company.

The Merry Brothers Brick and Tile Company (hereinafter called Merry) is engaged in the business of mining clay, from which it manufactures burnt brick or tile, by applying the following processes (*Merry* R. 57-59):

(a) The clay is mined at several different pits simultaneously by draglines and loaded in dump cars which operate on railroad tracks and carry the clay to the plant.

(b) The clay is dumped from the cars into large feeders which mix the clay and reduce the large

chunks to a size that can be carried on a conveyor belt.

(c) The clay mined from the several different pits is discharged from the feeders on conveyor belts which carry it first to a disintegrator or crusher and then a storage shed, where it is blended and weathered.

(d) The clay blended and weathered in the storage shed is then loaded onto a conveyor belt which carries the clay to a set of smooth roll crushers, which further reduce the size of the chunks. In one of the plants there are two small additional granulators, or pug mills, through which the clay passes before reaching the smooth roll crushers.

(e) From these smooth roll crushers the clay is discharged onto another conveyor belt, which carries it by belt conveyors to another feeder where the clay is further blended or mixed.

(f) From the feeder the clay is discharged into the pug mill, which is a part of the brick machine wherein water is added as the final tempering process.

(g) From the pug mill the clay passes through a sealing die into and through a vacuum chamber where air is evacuated from the clay by a vacuum pump. The clay then falls into the extrusion section of the machine, where it is forced under pressure through various shapes of dies in long ribbons.

(h) The long ribbons of clay as extruded through the dies pass into the cutting machine, which cuts them into clay units of the desired size or length.

(i) The clay units as cut pass onto a conveyor belt and are then stacked by hand on dryer cars. These cars of brick are then moved to the dryer tunnels, where free water is evaporated from the clay units by warm air from fans which is blown on and over the units.

(j) When the free water is thus removed, the clay units are stacked either in periodic kilns, semi-continuous kilns, or continuous tunnel kilns.

(k) The clay units are then burned, either in periodic, semi-continuous or continuous tunnel kilns.

(l) The burnt brick and tile are then removed from the kilns.

(m) After they have been removed from the kilns, the burnt brick and tile are sorted and then loaded for shipment to purchasers.

In its returns for 1951, 1952, and 1953, Merry computed and deducted as percentage depletion five percent of the entire sales price of the finished burnt brick and tile. The Commissioner of Internal Revenue, in order to compute the allowable basis for depletion, *i.e.*, the gross income from mining, classified the foregoing processes in two groups, "Mining" and "Manufacturing". Processes (a) through (e), listed above, were placed in the "Mining" group and the remaining processes in the "Manufacturing" group. The Commissioner computed Merry's gross income from mining by dividing the direct mining costs by the total costs of mining and manufacturing, based upon the foregoing classification, and then multiplying the resulting percentage by the total gross income. The resulting amount, it was determined, represented that portion of

the total gross income allocable to mining, and five percent thereof was allowed as a depletion deduction. (*Merry* R. 12-14, 22, 56-57.)

In accordance with these computations, the Commissioner determined deficiencies in income and excess profits taxes for 1951 and 1952, and income taxes for 1953. Merry paid the deficiencies, with adjustments, and for the year 1954 it computed depletion and paid its tax liability on the same basis which the Commissioner determined should have been used in computing the allowable depletion for the prior years. Merry then filed claims for refund for the years 1951-1954 inclusive; the claims were denied, and suit for refund followed. The District Court overruled the Commissioner's determination and entered judgment for Merry in the principal amount of $361,932.06 plus interest. (*Merry* R. 6-7, 21, 54, 63-65.) The Court of Appeals affirmed. (Appendix A, *infra*, pp. 23-30.)

Reliance Clay Products Company:

The Reliance Clay Products Company (hereinafter called Reliance) is engaged in the business of mining clay, from which it manufactures burnt brick or tile by applying substantially the same processes as set forth above in the case of Merry. (*Reliance* R. 77-78, 86-88.)

In its income tax returns for the years 1951 and 1952, Reliance computed and deducted percentage depletion on the basis of the entire sales price of the finished burnt brick and tile. The Commissioner determined the allowable depletion by classifying the processes as between mining and manufacturing, and by allocating the gross income from the sales of the burnt brick and

tile on the basis of such classification, in substantially the same manner as in the *Merry* case. (*Reliance* R. 83-86, 88-91.)

Reliance paid the resulting deficiencies and filed claims for refund, which were denied, and suit for refund followed. (*Reliance* R. 81-83.) The District Court overruled the Commissioner's determination and entered judgment for the taxpayer in the amounts of $22,944.20 and $3,228.61 for 1951 and 1952, respectively, plus interest. (*Reliance* R. 75-76.) The Court of Appeals affirmed. (Appendix A, *infra*, pp. 23-30.)

Companion cases.

The facts and issues in the remaining cases are in all material respects the same as in the *Merry* and *Reliance* cases. Accordingly, the parties stipulated, in all but the last four above-styled cases (see p. 2, note 3, *supra*), that in the event the Court of Appeals for the Fifth Circuit affirmed the decisions in *Merry* and *Reliance*, decisions were to be entered forthwith in favor of the taxpayers. After the entry of judgment in favor of taxpayers in *Merry* and *Reliance*, the Court of Appeals entered judgments in favor of taxpayers in the stipulated cases. (Appendix A, *infra*, pp. 30-37.) In the four remaining companion cases (*United States* v. *Teague Brick & Tile Co.*, *United States* v. *Cherokee Brick & Tile Co.*, *United States* v. *Burns Brick Co.*, and *United States* v. *Texas Vitrified Pipe Co.*), the parties stipulated, subsequent to the decisions in *Merry* and *Reliance*, for entry of judgment in favor of taxpayers, and the Court of Appeals entered judgment accordingly. (Appendix A, *infra*, pp. 37-40.)

REASONS FOR GRANTING THE WRIT

1. These cases present in common an important question of statutory construction, affecting the collection of hundreds of millions of dollars of revenue. Sections 23(m) and (n) and 114(b)(4) (Appendix B, *infra*, pp. 41-44) authorize a deduction for depletion of natural mineral deposits, measured by a percentage of the mine owner's "gross income from the property", which is defined as "the gross income from mining". The term "mining" is defined as including "not merely the extraction of the ores or minerals from the ground but also the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product".[4] Broadly stated, the problem is whether, for purposes of computing allowable percentage depletion, income from "mining" may include income derived from manufacturing or other non-mining activities. More particularly, the issue is whether manufacturing operations carried on by a mine owner in order to convert his mineral product into a manufactured product may properly be considered "ordinary treatment processes normally applied * * * to obtain the commercially marketable mineral product", within the purview of the statute.

The taxpayers in the instant cases mine clay, from which they ultimately produce burnt brick and tile, and then sell the finished manufactured products.[5] In com-

[4] Together with the transportation of the mineral to the plants or mills in which the ordinary treatment processes are applied, within specified mileage limits.

[5] After the clay is mined, it is carried to an adjacent plant, where it is mixed, reduced in size, and screened into a machine (pug mill) in which water is added as a final tempering process. The clay is

puting and deducting the percentage allowance for depletion[6] taxpayers used as a basis the gross income (sales price) realized from the finished products. The Commissioner determined deficiencies on the ground that "the gross income from mining" (the statutory basis on which percentage depletion is allowable for mineral deposits) is confined to income attributable to mining operations, and does not extend to income attributable to manufacturing operations. Applying the principles and formula embodied in the long-standing Treasury Regulations,[7] the Commissioner allocated the

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then passed into a brick machine, first entering an evacuation chamber where air is evacuated from the clay by a vacuum pump, and then an extrusion section where it is forced through various types of dies onto long ribbons. The ribbons are then passed into a cutting machine which cuts them into units of the desired size. These units are then moved to dryer tunnels, where the water is evaporated therefrom by open gas fires. They are then burned in kilns by natural gas fires, and the resulting burnt brick and tile is then removed and loaded for shipment.

[6] The percentage of "gross income from the property" allowable as a depletion deduction varies with different types of minerals. See Section 114(b)(4)(A). In 1951, brick and tile clay, and fire clay, were added to the category of mineral deposits for which percentage depletion is deductible, the percentages allowable being five and fifteen percent, respectively. See Section 319 of the Revenue Act of 1951, c. 521, 65 Stat. 452.

[7] Section 29.23(m)-1(f) of Treasury Regulations 111, as amended by T.D. 5413, 1944 Cum. Bull. 124 (Appendix B, *infra*, pp. 49-52), which reads in part as follows:

> If the taxpayer sells the crude mineral product of the property in the immediate vicinity of the mine, "gross income from the property" means the amount for which such product was sold, but, *if the product is* transported or *processed (other than by the ordinary treatment processes described below) before sale, "gross income from the property" means* the *representative market or field price* as of the date of sale of a mineral product of like kind and grade *as beneficiated by the ordinary treatment processes actually applied*, before transportation of such product. *If there is no such representative*

total amount realized by the taxpayers from the sale of the finished products as between their mining and manufacturing operations, and allowed percentage depletion on the basis of the income allocable to mining.

Rejecting the Commissioner's interpretation of the statute as embodied in the Regulations, and reaffirming its prior decision in *United States v. Cherokee Brick & Tile Co.*, 218 F. 2d 424, the court below has construed the statute as authorizing percentage depletion deductions on the basis of the entire sales proceeds of the finished manufactured product, notwithstanding the fact that a substantial portion of the proceeds reflects a return of, and is attributable to, the costs of what are patently manufacturing and other non-mining operations. In effect, the court has held that the depletion base prescribed by Congress ("the gross income from mining") extends to the total price received for a synthetic product resulting from *any and all processes* applied by the mine owner in transforming the mineral deposit into an end product sold, simply because the first commercially marketed product is the end product.[8]

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market or field price (as of the date of sale), *then there shall be used in lieu thereof the* representative market or field *price of the first marketable product* resulting from any process or processes (or, if the product in its crude mineral state is merely transported, the price for which sold) *minus the costs and proportionate profits attributable to* the transportation and *the processes beyond the ordinary treatment processes*. [Emphasis supplied.]

[8] Reiterating its position in the *Cherokee* case, the court below stated (Appendix A, *infra*, pp. 24-25):

> The statutory language is clear and unambiguous, which is that gross income from mining must include the income from ordinary treatment processes which must be applied to the ore or mineral in order to obtain the commercially marketable mineral product, that is, the first product which is marketable

While the *Cherokee* and the instant cases involve the proper statutory basis for depletion of certain types of clay (brick and tile and fire clays), the holding below appears broad enough to encompass a number of other mineral deposits for which percentage depletion is allowable. See Section 114(b)(4)(A). Indeed, the holding has been followed by three other Courts of Appeals, and it has been extended to two other classes of mineral deposits (talc and cement rock).[9] If permitted to stand, the decision below will result in the loss of a very substantial amount of revenue which the Treasury, under its established interpretation of the statute, has consistently regarded as properly payable by mine owners. The Acting Commissioner of Internal Revenue has advised the Department of Justice that a survey conducted by the Internal Revenue Service (see Appendix C, *infra*, pp. 57-60) indicates that (1) there are at least 370 cases now in litigation or pending administratively, involving similar minerals (clay, talc, cement rock and lime), in which taxpayers are attempting to apply the rule adopted by the court below to their own integrated mining-manufacturing operations for the years 1951-1954 in order to obtain the broad depletion base and the larger depletion allow-

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in commerce. There is no provision in the statute for excluding any process before such a marketable product is reached. The only restriction is that the processes must be the ordinary treatment processes normally applied by mine owners or operators.

[9] The rule was extended by the Fourth Circuit to talc (*Townsend v. Hitchcock Corp.*, 232 F. 2d 444) and by the First Circuit to cement rock (*Dragon Cement Co. v. United States*, decided May 14, 1957). And it has been applied by the Tenth Circuit in the case of brick and tile clay (*United States v. Sapulpa Brick & Tile Corp.*, 239 F. 2d 694). The Government is also filing a petition for a writ of certiorari in the *Dragon Cement* case.

ances which will thereby result; (2) the tax loss which would result from an application of the rule to these contested cases approximates $116,000,000; (3) the continued application of the rule to these minerals would result in an annual revenue loss of at least $49,000,000 for each succeeding taxable year; (4) attempts have been made, in the form of claims for the years 1951 through 1954, to apply the rule to nineteen other minerals covered by the statute;[10] and (5) if the rule is applicable to these other minerals, the tax loss resulting from such claims will approximate $17,476,869 and the potential recurring revenue loss will approximate an additional $39,523,040 per year. Moreover, it is the opinion of the Commissioner of Internal Revenue, based upon the numerous attempts already made to extend the rule to other minerals, that it is not unreasonable to expect that similar attempts will be made, based on alleged similarities to the minerals here involved, to apply the rule to additional minerals listed under Section 114(b)(4), with an inevitable increase in litigation and potential revenue loss. (Appendix C, *infra*, p. 58.) And since the percentage depletion provisions of the Internal Revenue Code of 1954 (Sections 611 and 613 (Appendix B, *infra*, pp. 44-48)) are substantially the same as those of the 1939 Code, the question is a recurring one and will continue in future years to have great importance in the administration of the taxing statute.

2. In holding that percentage depletion is allowable on the basis of the *total* gross income realized by a mine owner from integrated mining-manufacuring operations, including the portions allocable to the manufac-

[10] These claims are being contested.

turing processes, the court below extended the depletion allowance beyond the boundaries envisioned by Congress.

The court below disagreed with the Treasury's interpretation, which applies the allowable percentage solely to the gross income allocable to the mining activities, on the theory that it was contrary to the "clear and unambiguous" language of the statute. (Appendix A, *infra*, p. 24.) We submit that the administrative interpretation is in harmony with the congressional purpose and that in no event are the Treasury Regulations so plainly inconsistent with the statute as to warrant their nullification by the courts. See *Commissioner* v. *South Texas Co.*, 333 U.S. 496, 501; *Fawcus Machine Co.* v. *United States*, 282 U.S. 375, 378; *Lykes* v. *United States*, 343 U.S. 118, 127. Certainly, the legislative intent cannot be said to be so free from doubt—as the court below assumed—as to leave no room for administrative interpretation.

Analysis of the basic nature and purpose of the percentage depletion provisions, their terms, and their legislative and administrative history, shows that the depletion base ("gross income from mining") contemplated by Congress has reference to income received from a mineral product resulting from a definite pattern of treatment processes, *i.e.*, concentration or purification processes which are proximately related to mining operations. Contrary to the view of the court below, Congress did not propose that the depletion base be measured by the value of a synthetic, manufactured product which was the result of any and all processes necessary to bring the mineral to a point of marketability.

(a) The allowance of a deduction for depletion is simply a recognition by Congress that a mineral deposit will become exhausted as a consequence of its removal from the earth in the course of a mining operation, and that the mine owner is entitled to recovery of his capital investment in the deposit. This has been the basic purpose of the depletion allowance from the beginning (*Stanton* v. *Baltic Mining Co.*, 240 U.S. 103; *Von Baumbach* v. *Sargent Land Co.*, 242 U.S. 503; *Burnet* v. *Harmel*, 287 U.S. 103), and it remains so today (*Kirby Petroleum Co.* v. *Commissioner*, 326 U.S. 599). As this Court said in the *Kirby* case, p. 603, percentage depletion is designed to provide for "the restoration of the taxpayer's capital". To confine the basis upon which percentage depletion is to be measured to the gross income derived from mining operations merely effectuates the underlying purpose of the deduction.

(b) The language of the statute, read as a whole, also supports the Treasury's interpretation. If, as the court below assumed, Congress wished to make the entire sales proceeds of the first marketable product the basis for computing percentage depletion on the mined property—irrespective of whether manufacturing processes are superimposed upon the mining processes in producing the property sold—it could readily and simply have said so. There would have been no need for Congress to define "gross income from the property" as "the gross income *from mining*", and in turn to define the term "mining" as including "ordinary *treatment* processes normally applied by mine owners or operators in order to obtain the commercially marketable *mineral* product". (Emphasis supplied.) Nor would there have been any need for Congress to elaborate the definition by specifying the particular

processes includable in the category of "treatment processes" and others which are excludable. That Congress used such qualifying language to define "gross income from the property" furnishes strong indication, in and of itself, that the stage at which a product is marketed or becomes commercially marketable was not meant to be the exclusive test for determining the depletion base.

(c) The legislative and administrative history of the statutory provisions in question further supports the Treasury's interpretation. Prior to the Revenue Act of 1943, the provisions governing percentage depletion [11] did not define the term "gross income from the property" to which the percentage was to be applied. Congress deemed it best, in dealing with the highly technical factors entering into the depletion allowance, to write the Act as simply as possible and to leave the technical features for administrative regulations.[12] Regulations were promulgated under the 1933 Act defining "gross income from the property" as the selling price of the "crude mineral product". If the crude mineral product was not sold as such but was further processed, "gross income from the property" meant the field price *before* the application of any processes (other than crushing, grinding or purification processes) to which the crude mineral product may have been subjected. In the event that no representative field price existed for the crude mineral product after the purification processes, a hypothetical field price was

[11] Section 204(c)(2) of the Revenue Act of 1926, c. 27, 44 Stat. 9; Sections 23(l), 114(b)(3) and (4) of the Revenue Act of 1932, c. 209, 47 Stat. 169.

[12] See Section 23(l) of the Revenue Act of 1932, *supra*, and similar provisions of later Acts, delegating to the Commissioner authority to issue Regulations providing for a "reasonable allowance" for depletion.

to be calculated; this was to be done by taking the first marketable product, regardless of the nature of the product or the processes to which it had been subjected, and deducting therefrom amounts allocable to processes beyond the allowable ones. Treasury Regulations 77, promulgated under the Revenue Act of 1932, Article 221(g).

In 1943 Congress added Section 114(b)(4)(B) (the provision here applicable) to the 1939 Code.[13] This section defined "*gross income from the property*" as "the *gross income from mining*", with "mining" being defined as including "the *ordinary treatment processes* normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products". (Emphasis supplied.) The administrative background which led to this refinement of the definition shows that Congress was primarily concerned not with the marketability of the mineral product, but with the nature of the processes which were to be considered "mining" processes. Under its Regulations, the Treasury Department had been treating all substantially equivalent concentration or purification processes as mining processes, whether or not specifically listed in the Regulations, but, some time prior to 1943, it began disallowing many purification processes even though they were similar in function to those specified in the Regulations. This was brought to the attention of Congress,[14] which responded by enacting the 1943 provision

[13] Section 124(c) of the Revenue Act of 1943, c. 63, 58 Stat. 21.

[14] See the testimony of Donald H. McLaughlin, Senate Hearings before the Committee on Finance, 78th Cong., 1st Sess., on Revenue Act of 1943, pp. 527-529. See, also, testimony of Robert M. Searls, representing the California Chapter of The American Mining Congress (1 House Hearings before the Committee on Ways and Means, 77th Cong., 2d Sess., on Revenue Revision of 1942, pp. 1199-1202).

in question. Insofar as the includable "processes" are concerned, the provision is virtually identical in pattern with the then existing Regulations, *i.e.*, the includable processes consist of *treatment* processes which are characteristic of *mining* as distinguished from manufacturing operations. Indeed, the Senate Finance Committee Report, at the time of the enactment of this provision, stated (S. Rep. No. 627, 78th Cong., 1st Sess., pp. 23-24 (1944 Cum. Bull. 973, 992)) that "[t]he definition here prescribed * * * is in accord with the original regulations and the Bureau practices and procedures thereunder." That the 1943 amendment was intended to codify the Regulations issued under the 1932 Act is confirmed by the fact that it was made retroactive to 1932.[15]

The Treasury Regulations under the 1939 Code which the Commissioner here applied and the court below viewed as invalid contain essentially the same provisions as the predecessor Regulations in terms of the nature and scope of the processes which may be treated as "mining" processes. And when Congress in 1951 added brick and tile clay and fire clay to the categories of minerals for which percentage depletion may be deducted,[16] the Commissioner merely applied the provi-

[15] Section 124 (d) of the Revenue Act of 1943, *supra*. See, also, S. Rep. No. 2375, 81st Cong., 2d Sess., p. 53 (1950-2 Cum. Bull. 483, 522). Nothing in the legislative or administrative history justifies the supposition of the court below (Appendix A, *infra*, pp. 26, 27, 28-29) that Congress was only seeking a "simple, practical rule" for computing percentage depletion, based solely upon the marketability of a product, regardless of the nature of the processes which were applied to obtain the product. The congressional inquiry at the time of the enactment of the provision was directed toward the processes involved, and the prior administrative practice which Congress approved always considered the nature of the processes involved to be significant.

[16] Section 319 of the Revenue Act of 1951, c. 521, 65 Stat. 452.

sions of the Regulations to determine the gross income derived from the mining of clay.

The applicable Regulations were issued shortly after the 1943 addition to the 1939 Code of the statutory provision in question (Section 114(b)(4)(B)). This Court has "many times declared that Treasury Regulations must be sustained unless unreasonable and plainly inconsistent with the revenue statutes and that they constitute contemporaneous constructions by those charged with administration of these statutes which should not be overruled except for weighty reasons" (*Commissioner* v. *South Texas Co.*, 333 U.S. 496, 501). This established principle applies with special force where, as here, the subject matter is technical and complex, calling for knowledge of mineralogy and mineralogical processes. See *Helvering* v. *Wilshire Oil Co.*, 308 U.S. 90, 103. Furthermore, since the time that the Regulations were promulgated (1944), Congress has several times extensively amended the 1939 Code without changing the provision to which the Regulations are addressed. Under equally familiar rules governing the construction of taxing statutes, the Treasury's interpretation must be deemed to have received implied legislative approval by virtue of substantial re-enactment of the statute. *Lykes* v. *United States*, 343 U.S. 118, 129; *Commissioner* v. *Flowers*, 326 U.S. 465, 469. The most that may be argued in taxpayers' favor is that the statute in question is ambiguous and hence susceptible of more than one reasonable interpretation. The Treasury's interpretation cannot be said to be any less reasonable, however, than the one advanced by taxpayers and adopted by the court below. Where a statute is susceptible of different reasonable interpreta-

tions, the construction adopted by the agency responsible for its administration should be accepted by the courts. *United States* v. *Allen-Bradley Co.*, 352 U.S. 306; *Commissioner* v. *South Texas Co.*, *supra*. See *Unemployment Comm'n* v. *Aragon*, 329 U.S. 143. The court below erred in disregarding these basic principles of statutory construction.

3. The decision below produces grave inequities within and among classes of taxpayers. The depletion deduction provisions, no less than other tax deduction provisions, are matters of legislative grace which must be strictly construed,[17] particularly where, as here, the deduction runs in favor of a selected group of taxpayers, namely, those whose income-producing activities consist of mining. To reduce further the tax liability of a particular member of that group by extending the special percentage depletion allowance to gross income derived from his manufacturing activities, solely because he chooses to combine such activities with his mining activities, not only accords him preferential tax treatment *vis-a-vis* other members of the group; it also places an unfair additional tax burden upon taxpayers who engage solely in manufacturing activities, and, indeed, upon all other classes of taxpayers.[18]

[17] *United States* v. *Olympic Radio & Television*, 349 U.S. 232, 235-236; *Deputy* v. *duPont*, 308 U.S. 488, 493; *New Colonial Co.* v. *Helvering*, 292 U.S. 435, 440.

[18] Moreover, the decision below permits miners of brick and tile clay to control the extent of the depletion allowance by electing to manufacture the more expensive burnt brick and tile products, such as face brick, colonial flash brick, and other special forms of burnt brick, and thus obtain a broader depletion base than those who manufacture and sell the cheaper forms of common brick, although they both use the identical amount of the crude mineral, brick and tile clay.

No valid reason appears, and none is suggested by the court below, for imputing to Congress an intent to accord to mine owners who engage in integrated mining-manufacturing activities a depletion allowance based upon gross income derived from their non-mining activities, and thus to single out these taxpayers for preferred tax treatment. Even if the legislative intent in this respect were not as plain as we submit it is; "[a] desire for equality among taxpayers is to be attributed to Congress, rather than the reverse". *Colgate Co.* v. *United States*, 320 U.S. 422, 425.

4. Quite apart from the inequitable results it otherwise produces, the decision below ignores the repeated admonitions of this Court that the federal revenue laws are to be interpreted "so as to give a uniform application to a nationwide scheme of taxation". *Burnet* v. *Harmel*, 287 U.S. 103, 110; *United States* v. *Gilbert Associates*, 345 U.S. 361, 364; *Lyeth* v. *Hoey*, 305 U.S. 188, 194; *United States* v. *Pelzer*, 312 U. S. 399, 402-403. In holding that "ordinary treatment processes", as that phrase is used in Section 114(b)(4)(B), embraces any and all processes applied by a mine owner up to a point where the product becomes commercially marketable, including processes which are essentially manufacturing in character, the court below overlooked the economic fact that the stage of marketability may and often does vary from mineral to mineral and, even as respects the same mineral, from area to area. Under the reasoning of the court below, the statutory basis for percentage depletion ("gross income from mining") will differ markedly as between taxpayers who mine one type of mineral

rather than another,[19] and as between taxpayers who, although they are engaged in mining the same type of mineral, do their mining in different localities.[20] Indeed, under the rationale of the opinion below, it has been held that the very same taxpayer may use different depletion bases with respect to the same class of mineral merely because the mineral was extracted from two separate mines.[21] No such incongruous results were intended by Congress. "A cardinal principle of Congress in its tax scheme is uniformity, as far as may be" (*United States* v. *Gilbert Associates*, *supra*, p. 364). That principle is fully applicable here.

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[19] It is undisputed, and Section 114(b)(4)(B) (iv.) explicitly provides, that in the case of certain metals and ores "which are not customarily sold in the form of the crude mineral product", the term "ordinary treatment processes" includes only designated processes ("crushing, grinding and beneficiation by concentration * * * or by substantially equivalent processes"); additional processes applied in order to convert the crude mineral product into a marketable product are not specified as includable. The decisions below, on the other hand, accord miners of brick and tile clay favored treatment by permitting them to include any and all processes applied to obtain the finished marketable product.

[20] For example, in two of the instant cases (*United States* v. *Acme Brick Co.*, and *United States* v. *Elgin-Butler Brick Co.*) involving fire clay, mined in Texas, the first commercial product was not reached until the mineral had been converted into burnt brick and tile. Yet in other geographical areas (*e.g.*, California, Colorado, Illinois, Indiana, Missouri, Ohio, and Pennsylvania) the first commercially marketable product is the crude fire clay itself. See the *Minerals Yearbook*, 1951, United States Department of Interior, Bureau of Mines, pp. 293-295.

[21] See *Riverton Lime and Stone Co.* v. *Commissioner*, 28 T.C. No. 49.

CONCLUSION

For the foregoing reasons, this petition for a writ of certiorari should be granted.

Respectfully submitted,

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JUNE 1957.

* See footnote 2, *supra*.

APPENDIX A

IN THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

No. 16373

UNITED STATES OF AMERICA, APPELLANT

versus

MERRY BROTHERS BRICK AND TILE COMPANY, APPELLEE

Appeal from the United States District Court for the Southern District of Georgia

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No. 16323

UNITED STATES OF AMERICA, APPELLANT

versus

RELIANCE CLAY PRODUCTS COMPANY, APPELLEE

Appeal from the United States District Court for the Northern District of Texas

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(March 27, 1957)

Before HUTCHESON, Chief Judge, and RIVES and BROWN, Circuit Judges

HUTCHESON, Chief Judge:

These appeals from judgments of the United States District Court for the Northern Districts of Georgia [1]

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[1] Dated July 3, 1956, opinion reported 145 F. Supp. p. 186.

and Texas,[2] respectively, involve claims for refund of income and excess profits taxes. They present on the same basic facts the same basic question, and have therefore been submitted and argued together.

This quesion is whether this court will depart from its decision in *U.S. v. Cherokee Brick & Tile Co.*, 218 F(2) 424, in which, affirming the judgment and approving the opinion of the United States District Court for the Middle District of Georgia, in *Cherokee Brick & Tile Co. v. United States*, 122 F. Sup. 59, we said, at pages 424-25, of the pertinent portion of Sec. 114[3] of the Internal Revenue Code:

> "The statutory language is clear and unambiguous, which is that gross income from mining must include the income from ordinary treatment processes which must be applied to the ore or mineral in order to obtain the commercially marketable mineral product, that is, the first product which is marketable in commerce. There is no provision in the statute for excluding any process before such a marketable product is reached. The only restric-

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[2] Dated May 14, 1956, no written opinion.

[3] "(b). Basis for depletion

* * * * * * *

"(4) (A) The allowance for depletion under Sec. 23(m) in the case of the following mines and other natural deposits shall be—(i) in the case of * * * brick and tile clay * * * 5 per centum, * * * of the gross income from the property during the taxable year. * * *

"(B) Definition of gross income from property. As used in this paragraph the term 'gross income from the property' means the gross income from mining. The term 'mining' as used herein shall be considered to include not merely the extraction of the ores or minerals from the ground but also the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products, * * *"

tion is that the processes must be the ordinary treatment processes normally applied by mine owners or operators.

"The complaint alleges that, of the brick and tile clay mined in the United States, there is opportunity for the sale of only a negligible quantity before it is put into the form of burnt brick and tile. This allegation is admitted in the answer of the appellant. For this and other reasons (but mainly for this one) stated in the opinion of the district court, above cited, the judgment appealed from should be affirmed."

Conceding that the cases were decided below in accordance with our decision in the Cherokee case and that if that decision stands, they must be affirmed, the United States, stating: "Since this decision, the United States District Court of Maine, in *Dragon Cement Co. v. United States*, 144 F. Supp. 188", has, declining to follow the Cherokee decision, put forward an interpretation of its own of the statute, goes on to say:

"In view of this interpretation and the great number of decisions which have arisen within this circuit following the decision in Cherokee Brick & Tile Co., and which involve substantial amounts of revenue, the government respectfully asks this court to reconsider its decision."

Pointing out that, with the exception of that in the Dragon case, all of the numerous decisions in the district courts in this and other circuits and of the Courts of Appeals for the Fourth Circuit, in *Townsend v. The Hitchcock Corp.*, 232 F(2) 445, and the Tenth Circuit, in *U.S. v. Sapulpa Brick & Tile Co.*, . . . F(2) . . . , have agreed with and approved our decision, appellees insist that the grounds now put forward in support of its reconsideration present no sound reasons therefor.

They urge upon us moreover that if we should enter upon such a reconsideration of the decision, the result would only be to reaffirm it, since the undisputed facts and every sound consideration of statutory construction and application support indeed compel the conclusion that it was right and should be adhered to.

Upon the fullest and most careful re-examination and reconsideration of our decision in the Cherokee case, in the light of the records and the briefs and arguments in that case and these, we agree that this is so. Because it is and because in their decisions the district court, and this court dealt adequately and correctly with the question presented in it and here, we will not undertake to restate or further elaborate upon the reasons they gave but will content ourselves with saying that, upon the plain and simple consideration set down and for the reasons pointed up in the Cherokee case, we decline to depart from the decision in it, and, on its authority, affirm the judgments appealed from.

We think it not amiss, however, to say that we have taken particular note of and approve the comment in appellee Reliance Clay Products Company's brief.[4]

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[4] "As one of the principal reasons for asking this Honorable Court to overrule the Cherokee case, the Government cites a District Court decision from the District of Maine, Dragon Cement Co. v. United States, 144 F. Supp. 488, a case involving cement rock. The Court there held that the cement which the taxpayer sold was not the 'commercially marketable mineral product' within the meaning of Section 114(b)(4)(B), although it was shown that only negligible quantities of cement rock could be sold before it was put in the form of cement.

"The Court reached this conclusion by a curious process of reasoning. It stated that cement is not a 'mineral product' within the statute, because chemical reactions in the kiln change the cement rock into a 'synthetic product'. The Court held that 'the emphasis must here be upon the word "mineral" as a noun', and that, therefore, a 'mineral product' is a product 'still in a mineral state.'

"The Court thus rewrote the statute to refer to the 'commercially marketable mineral', rather than the 'commercially marketable

We have also taken particular note of and agree with Proposition No. 2 in Merry Brothers' brief, "*The government's attack on the Cherokee case is based on the fallacious assumption that the Cherokee decision allows depletion on 'manufacturing processes'*" (emphasis supplied), and its argument thereunder reproduced in part in the margin,[5] as well as its corrollary

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mineral product or products.' *Furthermore, it ignored completely the fact that Congress intended Section 114(b)(4)(B) to provide a simple marketable product rule to obtain the starting point for the computation of the percentage depletion deduction.* The Court in the Dragon Cement case recognized that, under its interpretation of 'mineral product', there never is a 'commercially marketable mineral product' obtained from cement rock. Thus the decision in the Dragon Cement case completely frustrates the purpose of Congress to provide the marketable product rule for computing the depletion deduction for all ores and minerals granted percentage depletion by Section 114(b)(4), including cement rock and brick and tile clay. * * *

"The Court in the Dragon Cement case ignored the plain obvious and generally understood meaning of 'mineral product' as will be shown below. It seized upon the word 'mineral' as the crucial word in the statutory phrase 'the commercially marketable mineral product or products.' That the word 'mineral' is not the crucial word in the statutory phrase is made clear by the Senate Finance Committee Report, quoted above, explaining the meaning of Sec. 114(b)(4)(B), which that Committee added to the Revenue Act of 1943:

> "The purpose of the provision is to make certain that the ordinary treatment processes which a mine operator would normally apply to obtain a *marketable product* should be considered as a part of the mining operation. * * *". (emphasis supplied) Sen. Rep. 627, 78th Cong., 1st Sess. p. 23.

"Although the draft of the bill to which this Report referred contained the word 'mineral' and the phrase was worded exactly the same as it was in the final Act, the Committee did not even mention the word 'mineral' in explaining that the purpose of the provision is to enable the mine operator to obtain a 'marketable product.'" (emphasis supplied).

[5] "The Government's basic argument is not related to the language of the statute, but rests rather upon the theory or 'concept' of depletion which, the Government asserts, Congress had in mind

"*that the Government's argument ignores the obvious fact that Congress intended Sec. 114(b)(4) to provide a simple, practical rule which could easily be applied to compute the percentage depletion deduction*" (emphasis supplied) and its argument in support reproduced in part here:

> "* * * we might also point out here that the Government's argument completely ignores the obvious fact that Congress intended Sec. 114(b)(4) to provide a simple, practical rule which could be

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when it granted the deduction. The Government argues, basically, that in the light of the theory of depletion it is unreasonable to suppose that Congress would have provided a deduction based on the gross income from the sale of 'manufactured' or 'finished' products such as brick and tile. The Government's brief undertakes to confuse the issue by giving the impression that the statute allows depletion on 'mining' or 'mining processes' and that this Court in the Cherokee case sustained a deduction for depletion not only on 'mining processes' but on 'manufacturing processes' or on a 'manufactured product'.

"Nothing could be further from the truth. Depletion is not allowed on any process, 'mining' or 'manufacturing', and is not allowed on any product. It is just as absurd to talk of allowing depletion 'on' the first 'mining' process of extracting clay from the ground, as it is to talk of allowing depletion 'on' the last 'manufacturing' process of burning the clay in the kiln. On the contrary, depletion is allowed to compensate the mine owner for exhaustion of his natural deposit. But instead of limiting the depletion deduction to a recovery of the cost of the natural deposit, Congress has chosen to allow the deduction to be computed as a stated percentage of the selling price of the 'commercially marketable mineral product', the selling price of the mineral product for which a commercial market exists. It has done so by defining 'gross income from the property' in Sec. 114(b)(4)(B) to include not only the income derived from the extraction process but also the income from processes applied to the ore or mineral, after extraction from the natural deposit, to obtain the commercially marketable mineral product. But in no sense does this mean that depletion is allowed 'on' any of the processes or 'on' the products produced thereby, or that such processes or products are 'depleted'. We feel that this simple analysis disposes of the Government's whole argument."

easily applied to compute the percentage depletion deduction.

"In order to compute a percentage depletion deduction, there must be a dollar base to which to apply the applicable percentage. Congress elected to use the marketable product rule as a simple means to provide this dollar base. With this dollar base established in Subparagraph (B) of Section 114(b)(4), Congress can then set the applicable rates in Subparagraph (A) to produce the dollar amount of depletion which it wishes to grant in the case of each particular type of natural deposit without disturbing the simple means for determining the dollar base. Of course, the processing necessary to obtain marketable products from the ores and minerals mined from the various types of natural deposits will vary greatly, but this fact can be taken into account in fixing the applicable rates. Thus, Congress has set rates in Sec. 114(b)(4)(A) which vary from 5% to 23%, and these rates can be raised or lowered as Congress sees fit.

"* * * If Congress upon further consideration should feel that applying the applicable rate to the gross income from any product, whether or not it is a 'manufactured' product, produces too large a depletion deduction, and should wish to decrease that deduction, it has only to lower the rate while still using as a base the gross income from the marketable product.

"In spite of its effort to conceal the fact, the Government's argument in sum and substance is merely that 5% of the selling price of burnt brick and tile is too large a deduction to allow the mine owner as compensation for that part of the brick and tile clay deposit consumed in producing that

brick and tile. However, the amount of the deduction to be allowed to the miners of brick and tile clay is a matter exclusively for Congress. The Government, therefore, recognizing that it cannot ask this court to change the rate of 5% specified in the statute for brick and tile clay, seeks instead to have this court rewrite the statute by changing the dollar base to which the rate is applied, as the court did in the Dragon Cement case."

The judgments are AFFIRMED.

[Original Filed—April 25, 1957]

IN THE UNITED STATES COURT OF APPEALS
FIFTH CIRCUIT

No. 16522

UNITED STATES OF AMERICA, APPELLANT,

versus

ESTATE OF L. L. STEPHENSON, THE FIRST NATIONAL BANK OF BIRMINGHAM, AS EXECUTOR, ET AL., APPELLEES.

Appeal from the United States District Court for the Northern District of Alabama

Before HUTCHESON, Chief Judge, and RIVES and BROWN, Circuit Judges.

By the COURT:

Pursuant to the Stipulation, and Order entered in the above entitled cause on March 8, 1957 that in the event

this Court affirms the decisions in *United States* v. *Reliance Clay Products Co.* (Docket No. 16323), and *United States* v. *Merry Brothers Brick and Tile Co.* (Docket No. 16373), then decision shall be entered forthwith in favor of the taxpayer in the above-entitled case, and it appearing that the judgment of the District Court in cases Nos. 16323 and 16373 were affirmed on March 27, 1957.

It is now here ordered and adjudged by this Court that the judgments of the said District Court in this cause be, and the same are hereby, affirmed.

[Original Filed—April 25, 1957]

IN THE UNITED STATES COURT OF APPEALS
FIFTH CIRCUIT

No. 16525

UNITED STATES OF AMERICA, APPELLANT,

versus

TUPELO BRICK AND TILE COMPANY, APPELLEES.

Appeal from the United States Distrit Court for the Northern District of Mississippi.

Before HUTCHESON, Chief Judge, and RIVES and BROWN, Circuit Judges.

By the COURT:

Pursuant to the Stipulation and Order entered in the above entitled cause on March 8, 1957 that in the event this Court affirms the decisions in *United States*

v. *Reliance Clay Products Co.* (Docket No. 16323), and *United States* v. *Merry Brothers Brick and Tile Co.* (Docket No. 16373), then decision shall be entered forthwith in favor of the taxpayer in the above-entitled case, and it appearing that the judgment of the District Court in cases Nos. 16323 and 16373 were affirmed on March 27, 1957,

It is now here ordered and adjudged by this Court that the judgment of the said District Court in this cause be, and the same is hereby, affirmed.

[Original Filed—April 25, 1957]

IN THE UNITED STATES COURT OF APPEALS
FIFTH CIRCUIT

No. 16547

UNITED STATES OF AMERICA, APPELLANT,

versus

ELGIN-BUTLER BRICK COMPANY, APPELLEE

Appeal from the United States District Court for the Western District of Texas.

Before HUTCHESON, Chief Judge, and RIVES and BROWN, Circuit Judges.

By the COURT:

Pursuant to the Stipulation and Order entered in the above entitled cause on March 28, 1957 that in the event this Court affirms the decisions in *United States* v. *Reliance Clay Products Co.* (Docket No. 16323),

and *United States* v. *Merry Brothers Brick and Tile Co.* (Docket No. 16373), then decision shall be entered forthwith in favor of the taxpayer in the above-entitled case, and it appearing that the judgment of the District Court in cases Nos. 16323 and 16373 were affirmed on March 27, 1957.

It is now here ordered and adjudged by this Court that the judgment of the said District Court in this cause be, and the same is hereby, affirmed.

[Original Filed—April 25, 1957]

IN THE UNITED STATES COURT OF APPEALS,
FIFTH CIRCUIT

No. 16562

PAUL COBB, DISTRICT DIRECTOR OF INTERNAL REVENUE, APPELLANT,

versus

CHATTAHOOCHEE BRICK COMPANY, APPELLEE

Appeal from the United States District Court for the Northern District of Georgia

Before HUTCHESON, Chief Judge, and RIVES and BROWN, Circuit Judges

By the COURT:

Pursuant to the Stipulation, and Order entered in the above entitled cause on March 8, 1957 that in the event this Court affirms the decisions in *United States* v. *Reliance Clay Products Co.* (Docket No. 16323), and *United States* v. *Merry Brothers Brick and Tile Co.*

(Docket No. 16373), then decision shall be entered forthwith in favor of the taxpayer in the above-entitled case, and it appearing that the judgment of the District Court in cases Nos. 16323 and 16373 were affirmed on March 27, 1957,

It is now here ordered and adjudged by this Court that the judgment of the said District Court in this cause be, and the same is hereby, affirmed.

[Original Filed—April 25, 1957]

IN THE UNITED STATES COURT OF APPEALS,
FIFTH CIRCUIT

No. 16563

UNITED STATES OF AMERICA, APPELLANT,

versus

ATLANTA BRICK AND TILE COMPANY, APPELLEE

Appeal from the United States District Court for the Northern District of Georgia

Before HUTCHESON, Chief Judge, and RIVES and BROWN, Circuit Judges

By the COURT:

Pursuant to the Stipulation, and Order entered in the above entitled cause on March 8, 1957 that in the event this Court affirms the decisions in *United States* v. *Reliance Clay Products Co.* (Docket No. 16323), and *United States* v. *Merry Brothers Brick and Tile Co.* (Docket No. 16373), then decision shall be entered

forthwith in favor of the taxpayer in the above-entitled case, and it appearing that the judgment of the District Court in cases Nos. 16323 and 16373 were affirmed on March 27, 1957,

It is now here ordered and adjudged by this Court that the judgment of the said District Court in this cause be, and the same is hereby, affirmed.

[Original Filed—April 25, 1957]

IN THE UNITED STATES COURT OF APPEALS,
FIFTH CIRCUIT

No. 16572

UNITED STATES OF AMERICA, APPELLANT,

versus

ACME BRICK COMPANY, APPELLEE

Appeal from the United States District Court for the Northern District of Texas

Before HUTCHESON, Chief Judge, and RIVES and BROWN, Circuit Judges

By the COURT:

Pursuant to the Stipulation, and Order entered in the above entitled cause on March 28, 1957 that in the event this Court affirms the decisions in *United States* v. *Reliance Clay Products Co.* (Docket No. 16323), and *United States* v. *Merry Brothers Brick and Tile Co.* (Docket No. 16373), then decision shall be entered forthwith in favor of the taxpayer in the above-entitled

case, and it appearing that the judgment of the District Court in cases Nos. 16323 and 16373 were affirmed on March 27, 1957,

It is now here ordered and adjudged by this Court that the judgment of the said District Court in this cause be, and the same is hereby, affirmed.

[Original Filed—April 25, 1957]

IN THE UNITED STATES COURT OF APPEALS,
FIFTH CIRCUIT

No. 16599

ELLIS CAMPBELL, DISTRICT DIRECTOR OF INTERNAL REVENUE SERVICE and UNITED STATES OF AMERICA, APPELLANTS,

versus

CARNEY KIRBY and WIFE, GENEVA KIRBY, ET AL., APPELLEES

Appeal from the United States District Court for the Northern District of Texas

Before HUTCHESON, Chief Judge, and RIVES and BROWN, Circuit Judges

By the COURT:

Pursuant to the Stipulation, and Order entered in the above entitled cause on March 8, 1957 that in the event this Court affirms the decisions in *United States* v. *Reliance Clay Products Co.* (Docket No. 16323), and *United States* v. *Merry Brothers Brick and Tile Co.* (Docket No. 16373), then decision shall be entered

forthwith in favor of the taxpayer in the above-entitled case, and it appearing that the judgment of the District Court in cases Nos. 16323 and 16373 were affirmed on March 27, 1957,

It is now here ordered and adjudged by this Court that the judgments of the said District Court in this cause be, and the same are hereby, affirmed.

[Original Filed—April 29, 1957]

IN THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

No. 16607

UNITED STATES OF AMERICA, APPELLANT

versus

TEAGUE BRICK & TILE COMPANY, APPELLEE

Appeal from the United States District Court for the Western District of Texas

Before HUTCHESON, Chief Judge, and RIVES and BROWN, Circuit Judges

By the COURT:

Pursuant to the Stipulation filed in the above entitled cause on April 16, 1957 that judgment be entered by this Court affirming the decision of the District Court in view of the decision of this Court in *United States v. Merry Brothers Brick and Tile Company* (Docket No. 16373) and *United States v. Reliance Clay Products Company* (Docket No. 16323), decided March 27, 1957,

It is now here ordered and adjudged by this Court that the judgment of the said District Court in this cause be, and the same is hereby, affirmed.

[Original Filed—May 3, 1957]

IN THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

No. 16,647

UNITED STATES OF AMERICA, APPELLANT

versus

CHEROKEE BRICK & TILE COMPANY, APPELLEE

Appeal from the United States District Court for the Middle District of Georgia

Before HUTCHESON, Chief Judge, and RIVES and BROWN, Circuit Judges

By the COURT

Pursuant to the Stipulation filed in the above entitled cause on May 3, 1957 that judgment be entered by this Court affirming the decision of the District Court in view of the decision of this Court in *United States v. Merry Brothers Brick and Tile Company* (Docket No. 16373) and *United States* v. *Reliance Clay Products Company* (Docket No. 16323), decided March 27, 1957.

It is now here ordered and adjudged by this Court that the judgment of the said District Court in this cause be, and the same is hereby, affirmed.

[Original Filed—May 3, 1957]

IN THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

No. 16,648

UNITED STATES OF AMERICA, APPELLANT

versus

BURNS BRICK COMPANY, APPELLEE

Appeal from the United States District Court for the Middle District of Georgia

Before HUTCHESON, Chief Judge, and RIVES and BROWN, Circuit Judges

By the COURT:

Pursuant to the Stipulation filed in the above entitled cause on May 3, 1957 that judgment be entered by this Court affirming the decision of the District Court in view of the decision of this Court in *United States* v. *Merry Brothers Brick and Tile Company* (Docket No. 16373) and *United States* v. *Reliance Clay Products Company* (Docket No. 16323), decided March 27, 1957.

It is now here ordered and adjudged by this Court that the judgment of the said District Court in Civil Actions Nos. 1276, 1285, 1326 & 1327, be, and the same is hereby, affirmed.

[Original Filed—May 10, 1957]

IN THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

No. 16,673

UNITED STATES OF AMERICA, APPELLANT

versus

TEXAS VITRIFIED PIPE COMPANY, APPELLEE

Appeal from the United States District Court for the Northern District of Texas

Before HUTCHESON, Chief Judge, and RIVES and BROWN, Circuit Judges

By the COURT:

Pursuant to the Stipulation filed in the above entitled cause on May 10, 1957 that judgment be entered by this Court affirming the decision of the District Court in view of the decision of this Court in *United States v. Merry Brothers Brick and Tile Company* (Docket No. 16373) and *United States v. Reliance Clay Products Company* (Docket No. 16323), decided March 27, 1957,

It is now here ordered and adjudged by this Court that the judgment of the said District Court in this cause be, and the same is hereby, affirmed.

Internal Revenue Code of 1939:

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

* * * * * *

(m) *Depletion.*—In the case of mines, oil and gas wells, other natural deposits, and timber, a reasonable allowance for depletion and for depreciation of improvements, according to the peculiar conditions in each case; such reasonable allowance in all cases to be made under rules and regulations to be prescribed by the Commissioner, with the approval of the Secretary. * * *

(n) *Basis for Depreciation and Depletion.*—The basis upon which depletion, exhaustion, wear and tear, and obsolescence are to be allowed in respect of any property shall be as provided in section 114.

* * * * * *

(26 U. S. C. 1952 ed., Sec. 23.)

SEC. 114. BASIS FOR DEPRECIATION AND DEPLETION.

* * * * * *

(b) *Basis for Depletion.*—

* * * * * *

(4) [as amended by Sec. 145 of the Revenue Act of 1942, c. 619, 56 Stat. 798, and Sec. 319 (a) of the Revenue Act of 1951, c. 521, 65 Stat. 452) *Percentage*

*age depletion for * * * certain other mines and natural mineral deposits—*

(A) *In general.*—The allowance for depletion under section 23 (m) in the case of the following mines and other natural deposits shall be—

(i) in the case of sand, gravel, slate, stone (including pumice and scoria), brick and tile clay, shale, oyster shell, clam shell, granite, marble, sodium chloride, and, if from brine wells, calcium chloride, magnesium chloride, and bromine, 5 per centum,

(ii) in the case of coal, asbestos, brucite, dolomite, magnesite, perlite, wollastonite, calcium carbonates, and magnesium carbonates, 10 per centum,

(iii) in the case of metal mines, aplite, bauxite, fluorspar, flake graphite, vermiculite, beryl, garnet, feldspar, mica, talc (including pyrophyllite), lepidolite, spodumene, barite, ball clay, sagger clay, china clay, phosphate rock, rock asphalt, trona, bentonite, gilsonite, thenardite, borax, fuller's earth, tripoli, refractory and fire clay, quartzite, diatomaceous earth, metallurgical grade limestone, chemical grade limestone, and potash, 15 per centum, and

(iv) in the case of sulfur, 23 per centum,

of the gross income from the property during the taxable year, excluding from such gross income an amount equal to any rents or royalties paid or incurred by the taxpayer in respect of the property. Such allowance shall not exceed 50 per centum of the net income of the taxpayer (computed without allowance for depletion) from the property, except that in no case shall the depletion allowance under section 23 (m) be less than it would

be if computed without reference to this paragraph.

(B) [as added by Sec. 124 (c) of the Revenue Act of 1943, c. 63, 58 Stat. 21, and amended by Sec. 207 (a) of the Revenue Act of 1950, c. 994, 64 Stat. 906, and Sec. 304 (d) of the Excess Profits Tax Act of 1950, c. 1199, 64 Stat. 1137] *Definition of Gross Income from Property.*—As used in this paragraph the term "gross income from the property" means the gross income from mining. The term "mining" as used herein shall be considered to include not merely the extraction of the ores or minerals from the ground but also the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products, and so much of the transportation of ores or minerals (whether or not by common carrier) from the point of extraction from the ground to the plants or mills in which the ordinary treatment processes are applied thereto as is not in excess of 50 miles unless the Secretary finds that the physical and other requirements are such that the ore or mineral must be transported a greater distance to such plants or mills. The term "ordinary treatment processes", as used herein, shall include the following: (i) In the case of coal—cleaning, breaking, sizing, and loading for shipment; (ii) in the case of sulphur—pumping to vats, cooling, breaking, and loading for shipment; (iii) in the case if iron ore, bauxite, ball and sagger clay, rock asphalt, and minerals which are customarily sold in the form of a crude mineral product—sorting, concentrating, and sintering to bring to shipping grade and form, and loading for shipment; and (iv) in the

case of lead, zinc, copper, gold, silver, or fluorspar ores, potash, and ores which are not customarily sold in the form of the crude mineral product—crushing, grinding, and beneficiation by concentration (gravity, flotation, amalgamation, electrostatic, or magnetic), cyanidation, leaching, crystallization, precipitation (but not including as an ordinary treatment process electrolytic deposition, roasting, thermal or electric smelting, or refining), or by substantially equivalent processes or combination of processes used in the separation or extraction of the product or products from the ore, including the furnacing of quicksilver ores. The principles of this subparagraph shall also be applicable in determining gross income attributable to mining for the purposes of sections 450 and 453.

* * * * *

(26 U. S. C. 1952 ed., Sec. 114.)

Internal Revenue Code of 1954:

SEC. 611. ALLOWANCE OF DEDUCTION FOR DEPLETION.

(a) *General Rule.*—In the case of mines, oil and gas wells, other natural deposits, and timber, there shall be allowed as a deduction in computing taxable income a reasonable allowance for depletion and for depreciation of improvements, according to the peculiar conditions in each case; such reasonable allowance in all cases to be made under regulations prescribed by the Secretary or his delegate. For purposes of this part, the term "mines" includes deposits of waste or residue, the extraction of ores or minerals from which is treated as mining under section 613 (c). In any case in

which it is ascertained as a result of operations or of development work that the recoverable units are greater or less than the prior estimate thereof, then such prior estimate (but not the basis for depletion) shall be revised and the allowance under this section for subsequent taxable years shall be based on such revised estimate.

* * * * *

(26 U. S. C. 1952 ed., Supp. II, Sec. 611.)

SEC. 613. PERCENTAGE DEPLETION.

(a) *General Rule.*—In the case of the mines, wells, and other natural deposits listed in subsection (b), the allowance for depletion under section 611 shall be the percentage, specified in subsection (b), of the gross income from the property excluding from such gross income an amount equal to any rents or royalties paid or incurred by the taxpayer in respect of the property. Such allowance shall not exceed 50 percent of the taxpayer's taxable income from the property (computed without allowance for depletion). In no case shall the allowance for depletion under section 611 be less than it would be if computed without reference to this section.

(b) *Percentage Depletion Rates.*—The mines, wells, and other natural deposits, and the percentages, referred to in subsection (a) are as follows:

(1) 27½ percent—oil and gas wells.

(2) 23 percent—

(A) sulfur and uranium; and

(B) if from deposits in the United States—anorthosite (to the extent that alumina and aluminum compounds are extracted therefrom), asbestos,

bauxite, beryl, celestite, chromite, corundum, fluorspar, graphite, ilmenite, kyanite, mica, olivine, quartz crystals (radio grade), rutile, block steatite talc, and zircon, and ores of the following metals: antimony, bismuth, cadmium, cobalt, columbium, lead, lithium, manganese, mercury, nickel, platinum and platinum-group metals, tantalum, thorium, tin titanium, tungsten, vanadium, and zinc.

(3) 15 percent—ball clay, bentonite, china clay, sagger clay, metal mines (if paragraph (2)(B) does not apply), rock asphalt, and vermiculite.

(4) 10 percent—asbestos (if paragraph (2)(B) does not apply), brucite, coal, lignite, perlite, sodium chloride, and wollastonite.

(5) 5 percent—

(A) brick and tile clay, gravel, mollusk shells (including clam shells and oyster shells), peat, pumice, sand, scoria, shale, and stone, except stone described in paragraph (6); * * *

* * * * *

(6) 15 percent—all other minerals (including, but not limited to, aplite, barite, borax, calcium carbonates, refractory and fire clay, diatomaceous earth, dolomite, feldspar, fullers earth, garnet, gilsonite, granite, limestone, magnesite, magnesium carbonates, marble, phosphate rock, potash, quartzite, slate, soapstone, stone (used or sold for use by the mine owner or operator as dimension stone or ornamental stone), thenardite, tripoli, trona, and (if paragraph (2)(B) does not apply) bauxite, beryl, flake graphite, fluorspar, lepidolite, mica, spodumene, and talc, including pyrophyllite), except that, unless sold on bid in direct competition with a bona fide bid to sell a mineral listed in paragraph (3), the percentage shall be 5 percent for any such other mineral when used, or sold for use, by the

mine owner or operator as rip rap, ballast, road material, rubble, concrete aggregates, or for similar purposes. For purposes of this paragraph, the term "all other minerals" does not include—

(A) soil, sod, dirt, turf, water, or mosses; or

(B) minerals from sea water, the air, or similar inexhaustible sources.

(c) *Definition of Gross Income from Property.*—For purposes of this section—

(1) *Gross income from the property.*—The term "gross income from the property" means, in the case of a property other than an oil or gas well, the gross income from mining.

(2) *Mining.*—The term "mining" includes not merely the extraction of the ores or minerals from the ground but also the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products, and so much of the transportation of ores or minerals (whether or not by common carrier) from the point of extraction from the ground to the plants or mills in which the ordinary treatment processes are applied thereto as is not in excess of 50 miles unless the Secretary or his delegate finds that the physical and other requirements are such that the ore or mineral must be transported a greater distance to such plants or mills.

(3) *Extraction of the ores or minerals from the ground.*—The term "extraction of the ores or minerals from the ground" includes the extraction by mine owners or operators of ores or minerals from the waste or residue of prior mining. The preceding sentence shall not apply to any such extraction of the mineral or ore by a purchaser of

such waste or residue or of the rights to extract ores or minerals therefrom:

(4) *Ordinary treatment processes.*—The term "ordinary treatment processes" includes the following:

(A) In the case of coal—cleaning, breaking, sizing, dust allaying, treating to prevent freezing, and loading for shipment;

(B) in the case of sulfur recovered by the Frasch process—pumping to vats, cooling, breaking, and loading for shipment;

(C) in the case of iron ore, bauxite, ball and sagger clay, rock asphalt, and minerals which are customarily sold in the form of a crude mineral product—sorting, concentrating, and sintering to bring to shipping grade and form, and loading for shipment;

(D) in the case of lead, zinc, copper, gold, silver, or fluorspar ores, potash, and ores which are not customarily sold in the form of the crude mineral product—crushing, grinding, and beneficiation by concentration (gravity, flotation, amalgamation, electrostatic, or magnetic), cyanidation, leaching, crystallization, precipitation (but not including as an ordinary treatment process electrolytic deposition, roasting thermal or electric smelting, or refining), or by substantially equivalent processes or combination of processes used in the separation or extraction of the product or products from the ore, including the furnacing of quicksilver ores; and

(E) the pulverization of talc; the burning of magnesite, and the sintering and nodulizing of phosphate rock.

(26 U.S.C. 1952 ed., Supp. IV, Sec. 613.)

Treasury Regulations 111, promulgated under the Internal Revenue Code of 1939:

Sec. 29.23(m)-1 [as amended by T.D. 5413, 1944 Cum. Bull. 124, and T.D. 6031, 1953-2 Cum. Bull. 120] *Depletion of Mines, Oil and Gas Wells, Other Natural Deposits, and Timber; Depreciation of Improvements.*—

* * * * * *

(f) The term "gross income from the property," as used in sections 114(b)(3) and 114(b)(4)(A) and sections 29.23(m)-1 to 29.23(m)-28, inclusive, means the following:

In the case of oil and gas wells, "gross income from the property" as used in section 114(b)(3) means the amount for which the taxpayer sells the oil and gas in the immediate vicinity of the well. If the oil and gas are not sold on the property but are manufactured or converted into a refined product prior to sale, or are transported from the property prior to sale, the gross income from the property shall be assumed to be equivalent to the representative market or field price (as of the date of sale) of the oil and gas before conversion or transportation.

In the case of a crude mineral product other than oil and gas, "gross income from the property," as used in section 114(b)(4)(A), means the gross income from mining. The term "mining" as used herein includes not only the extraction of ores or minerals from the ground but also the ordinary treatment processes which are normally applied by the mine owners or operators to the crude mineral product after extraction in order to obtain the commercially marketable mineral product or products.

If the taxpayer sells the crude mineral product of the property in the immediate vicinity of the mine, "gross income from the property" means the amount for which such product was sold, but, if the product is transported or processed (other than by the ordinary treatment processes described below) before sale, "gross income from the property" means the representative market or field price (as of the date of sale) of a mineral product of like kind and grade as beneficiated by the ordinary treatment processes actually applied, before transportation of such product. If there is no such representative market or field price (as of the date of sale), then there shall be used in lieu thereof the representative market or field price of the first marketable product resulting from any process or processes (or, if the product in its crude mineral state is merely transported, the price for which sold) minus the costs and proportionate profits attributable to the transportation and the processes beyond the ordinary treatment processes.

The term "ordinary treatment process," as used herein, shall include the following:

(1) In the case of coal—cleaning, breaking, sizing, and loading for shipment;

(2) In the case of sulphur—pumping to vats, cooling, breaking, and loading for shipment;

(3) In the case of iron ore, bauxite, ball and sagger clay, rock asphalt, and minerals which are customarily sold in the form of a crude mineral product—sorting, concentrating, and sintering (agglomerating by incipient fusion) to bring to shipping grade and form, and loading for shipment;

(4) In the case of lead, zinc, copper, gold, silver, or fluorspar ores, potash, and minerals which are not customarily sold in the form of the crude mineral product—crushing, grinding, and beneficiation by concentration (gravity, flotation, amalgamation, electrostatic, or magnetic), cyanidation; leaching, crystallization, precipitation, or by substantially equivalent processes or combination of processes used in the separation or extraction of the product or products from the mineral. The furnacing of quicksilver ores is included in the term "ordinary treatment processes." The following processes are not included in the term "ordinary treatment processes": electrolytic deposition, roasting, thermal or electric smelting, refining, or substantially equivalent processes.

In addition, the processes listed below are not included in the term "ordinary treatment processes" unless such processes are (i) otherwise provided for in (1), (2), (3), or (4) above; (ii) necessary or incidental to the processes provided for in (1), (2), (3), or (4) above; or (iii) necessary to bring the ores or minerals into condition or form suitable for shipment (for example, the agglomeration of concentrates):

(A) treatment effecting a chemical change,

(B) blending with other material,

(C) thermal action,

(D) fine pulverization, pressing into shape, or molding.

For the purposes of (3) and (4) above, the terms "concentration" or "concentrating" mean the process of eliminating waste or of separating two or more minerals or ores.

In case any of the ordinary treatment processes ar not applied in the immediate vicinity of the minin district in which the mine is located, costs incurre for transportation to the processing location and, i transported by the taxpayer, the proportionate profit attributable to transportation, should be subtracte from the sale price of the product to determine "gros income from the property."

In all cases there shall be excluded in determinin the "gross income from the property" an amount equa to any rents or royalties which were paid or incurre by the taxpayer in respect of the property and are no otherwise excluded from the "gross income from th property." If royalties in the form of bonus payment have been paid in respect of the property in the taxabl year or any prior years or if advanced royalties hav been paid in respect of the property in any taxable yea ending prior to December 31, 1939, the amount exclude from "gross income from the property" for the cur rent taxable year on account of such payments shall b an amount equal to that part of such payments whic is allocable to the product sold during the current tax able year. If advanced royalties have been paid in re spect of the property in any taxable year ending on o after December 31, 1939, the amount excluded fro "gross income from the property" for the current tax able year on account of such payments shall be a amount equal to the deduction for such taxable yea taken on account of such payments pursuant to sectio 29.23 (m)-10(e).

* * * * * *

Treasury Regulations 118, promulgated under th Internal Revenue Code of 1939:

Sec. 39.23 (m)-1. [As amended by T.D. 6059 1954-1 Cum. Bull. 80, and T.D. 6096, 1954-2 Cum

Bull. 69.] *Depletion of mines, oil and gas wells, other natural deposits, and timber; depreciation of improvements.*

* * * * * *

(c) As used in sections 114 (b) (3) and 114 (b) (4) (A) and §§ 39.23 (m)-1 to 39.23 (m)-19, inclusive, the term "gross income from the property" means the following:

* * * * * *

(2) In the case of a crude mineral product other than oil and gas, "gross income from the property," as used in section 114 (b) (4) (A), means the gross income from mining. The term "mining" as used herein includes not only the extraction of ores or minerals from the ground but also the ordinary treatment processes which are normally applied by the mine owners or operators to the crude mineral product after extraction in order to obtain the commercially marketable mineral product or products. The term "mining" as used herein also includes so much of the transportation of ores or minerals (whether or not by common carrier) from the point of extraction from the ground to the plants or mills in which the ordinary treatment processes are applied thereto as is not in excess of 50 miles, and, if the Commissioner finds that both the physical and other requirements are such that the ore or mineral must be transported a greater distance to such plants or mills, the transportation over such greater distance. * * *

(3) If the taxpayer sells the crude mineral product of the property in the immediate vicinity of the mine, "gross income from the property" means the amount for which such product was sold,

but, if the product is transported or processed (other than by the ordinary treatment processes described below) before sale, "gross income from the property" means the representative market or field price (as of the date of sale) of a mineral product of like kind and grade as beneficiated by the ordinary treatment processes actually applied, before transportation of such product (other than transportation treated, for the taxable year, as mining). If there is no such representative market or field price (as of the date of sale), then there shall be used in lieu thereof the representative market or field price of the first marketable product resulting from any process or processes (or, if the product in its crude mineral state is merely transported, the price for which sold) minus the costs and proportionate profits attributable to the transportation (other than transportation treated, for the taxable year, as mining) and the processes beyond the ordinary treatment processes. If the taxpayer establishes to the satisfaction of the Commissioner that another method of computation, other than the computation of profits proportionate to costs, clearly reflects the gross income from the property, then such gross income shall be computed by the use of such other method.

(4) In determining "gross income from the property", the sale price of the product shall not be reduced by the costs and proportionate profit attributable to the transportation which is treated for such taxable year as mining, that is, so much of the transportation of ores or minerals (whether or not by common carrier) from the point of extraction from the ground to the plants or mills in which the ordinary treatment processes are applied thereto as is not in excess of 50 miles (or, if the

Commissioner finds that both the physical and other requirements are such that the ore or mineral must be transported a greater distance to such plants or mills, such greater distance). Where such plants or mills are in excess of 50 miles (or of such greater distance) from the point of extraction from the ground, then costs incurred for transportation in excess of 50 miles (or of such greater distance) to the treatment plant and, if transported by the taxpayer, the proportionate profits attributable to such excess transportation should be subtracted from the sale price of the product to determine "gross income from the property". In the absence of methods which will clearly reflect costs of the various phases of transportation, the costs attributable to such excess transportation shall be an amount which is in the same ratio to the costs incurred for the total transportation to the treatment plant as the excess transportation is to such total transportation. If the taxpayer establishes to the satisfaction of the Commissioner that another method of computation other than the computation of profits proportionate to cost clearly reflects the gross income from the property, then such gross income shall be computed by the use of such other method.

* * * * * *

(f) (1) The term "ordinary treatment processes", as used in §§ 38.23(m)-1 to 39.23(m)-19, inclusive, shall include the following:

(i) In the case of coal—cleaning, breaking, sizing, and loading for shipment;

(ii) In the case of sulphur—pumping to vats, cooling, breaking, and loading for shipment;

sagger clay, rock asphalt, and minerals which are customarily sold in the form of a crude mineral product—sorting, concentrating, and sintering (agglomerating by incipient fusion) to bring to shipping grade and form, and loading for shipment;

(iv) In the case of lead, zinc, copper, gold, silver, or fluorspar ores, potash, and minerals which are not customarily sold in the form of the crude mineral product—crushing, grinding, and beneficiation by concentration (gravity, flotation, amalgamation, electrostatic, or magnetic), cyanidation, leaching, crystallization, precipitation, or by substantially equivalent processes or combination of processes used in the separation or extraction of the product or products from the mineral. The furnacing of quicksilver ores is included in the term "ordinary treatment processes". The following processes are not included in the term "ordinary treatment processes": electrolytic deposition, roasting, thermal or electric smelting, refining, or substantially equivalent processes.

(2) In addition, a treatment effecting a chemical change, the blending with other material, a thermal action, and the fine pulverization, pressing into shape or molding, are not included in the term "ordinary treatment processes" unless such processes are (i) otherwise provided for in subdivisions (i), (ii), (iii), or (iv) of subparagraph (1); (ii) necessary or incidental to the processes provided for in subdivisions (i), (ii), (iii), or (iv) of subparagraph (1); or (iii) necessary to bring the ores or minerals into condition or form suitable for shipment (for example, the agglomeration of

(iv) of subparagraph (1), the terms "concentration" or "concentrating" mean the process of eliminating waste or of separating two or more minerals or ores.

* * * * * *

APPENDIX C

U. S. TREASURY DEPARTMENT,
WASHINGTON 25

OFFICE OF COMMISSIONER OF INTERNAL REVENUE

Address reply to Commissioner of Internal Revenue
and refer to
CC:C:JEB
618418

June 11, 1957.

Hon. Charles K. Rice
Assistant Attorney General
Tax Division
Department of Justice
Washington 25, D. C.

In re: United States v. Merry Bros. Brick and Tile Co. and related cases. (C.A. 5th-No. 16373)

(Your file: CKR:ENS:SIF 5-20-181)

Dear Mr. Rice:

In connection with the recommendation of the office of the Chief Counsel that a petition for certiorari be filed in the above-entitled proceeding, this office completed a survey of cases in active litigation, those pending in the various District Directors' offices and those in the various Appellate Divisions, in an effort to ascertain the anticipated effect upon the revenue of following the rule of this decision in cases presently pending in litigation or administratively.

The results of this survey indicate that the immediate revenue loss which would result from some 451 cases either in litigation or pending at an administrative level for taxable years 1951 through 1955, wherein the rule of this decision was applied to 23 various min-

erals, may be expected to be approximately $134,000,000.00.

A conservative projection based upon current statutory provisions and statistics of income published for these 23 minerals or industries reflects an anticipated annual revenue loss for each succeeding taxable year resulting from industry-wide application of this rule of some $88,000,000.00.

In addition, consistent with the evident extension of this rule, it would appear that on the basis of alleged mining, engineering or economic similarities to these 23 minerals, it is not unreasonable to expect that like claims will be made in the future that barite, bromine, feldspar, graphite, iodine, magnesite and phosphate come under the rule expressed in this case, with an inevitable increase in litigation and attendant sizable loss of revenue.

This data emphasizes the serious importance of this issue from the standpoint of its present as well as its anticipated effect upon the revenue, upon the basis of which the office of the Chief Counsel has recommended that a petition for certiorari be filed in the above-entitled action.

Very truly yours,

(S.) O. GORDON DELK,
Acting Commissioner.

TABLE I

TAX DIFFERENTIAL, ATTRIBUTABLE TO CHEROKEE ISSUE AS REFLECTED CONTESTED CASES (IN LITIGATION AND PENDING ADMINISTRATIVELY) CLASSIFIED ACCORDING TO MINERALS, NUMBER OF CASES AND TAX INVOLVED.

Mineral	Number of Cases		Tax loss under Cherokee Rule	
Limestone (Cement & Lime)	62		88,486,176	
Clay (Brick & Tile)	281		18,082,200	
Fire Clay & China Clay	24		9,962,073	
Talc	3		35,380	
		370		116,565,829
Sodium Chloride	13		11,383,379	
Stone	32		2,828,302	
Dolomite	2		368,485	
Granite	5		204,500	
Shale	5		193,428	
Oyster Shells	1		25,563	
Potash	2		269,000	
Rare Earth Minerals	1		3,344	
Diatomaceous Earth	1		581,481	
Bauxite	1		102,600	
Fullers Earth	4		137,800	
Bentonite	2		69,500	
Calcium Carbonate	1		491	
Perlite	1		3,535	
Asbestos	1		38,274	
Lithium	1		216,000	
Gypsum	1		778,500	
Silica Sand	3		17,158	
Sand & Gravel	4		255,529	
		81		17,476,869
		451		134,042,698

Note: The above table shows only the tax loss to the government which results from the application of the Cherokee rule in 451 cases. The depletion deductions under the Internal Revenue Service rule as well as the Cherokee rule were not shown since information not available in 37 cases. The depletion deductions were available for 414 cases. In these cases the depletion deduction is 118,082,625 under the Internal Revenue Service Rule and 324,362,586 under the Cherokee Brick rule. The figure of $324,362,586 would be increased materially if the missing depletion data for 37 cases was included.

TABLE NO. 2

ESTIMATED TAX DIFFERENTIAL FOR THE MINERAL INDUSTRIES IN WHICH AT LEAST ONE TAXPAYER HAS APPLIED THE CHEROKEE RULE.

Name of Mineral	Depletion Rate %	Gross Income Under Internal Revenue (2) Service Rule	Gross Income Under Cherokee Rule (2)	Difference In Gross Income	Estimated Increase In The Depl. Deduction	Estimated Tax Differential (3)
Calcium Carbonate	10			Data unavailable		
Stone	5			Data unavailable		
Shale	5			Data unavailable		
Sodium Chloride	5	71,010,000	195,000,000	123,990,000	6,199,500	3,223,700
Silica Sand	5			Data not available		
Granite	5	2,000,000	3,000,000	1,000,000	50,000	26,000
Dolomite	10	4,000,000	25,965,000	21,965,000	2,196,500	1,142,180
Clay (Brick & tile)	5	31,180,000	321,891,000	290,711,000	14,535,500	7,558,460
Limestone (Cement)	10	128,610,000	638,512,000	509,902,000	50,990,200	26,514,904
Limestone (Lime)	15	32,292,000	95,231,000	62,939,000	9,440,850	4,909,242
Fire Clay	15	48,383,000	240,196,000	191,813,000	28,771,950	14,961,414
Perlite	10	873,054	7,997,731	7,126,677	712,668	370,587
Talc	15			Data not available		
Bauxite	15	16,776,000	14,605,000	3,829,000	574,350	298,662
Oyster Shells	5			Data not available		
Potash	15			Data not available		
Rare Earth Metals	15			Data not available		
Diatomaceous Earth	15	9,084,380	13,626,570	4,542,190	681,328	354,291
Asbestos	10	4,713,000	23,565,000	18,852,000	1,885,200	980,304
Gypsum (1)	15	22,896,000	224,923,000	202,027,000	30,304,050	15,758,106
Lithium	15	1,052,000	11,000,000	9,948,060	1,492,200	775,944
China Clay	15	25,206,000	175,000,000	14,794,000	22,469,100	11,683,932
Special Clays	15			Data not available		
TOTAL					170,303,496	88,557,818

Notes (1) Gypsum is not allowed percentage depletion under the 1939 Internal Revenue Code but is allowed percentage depletion based on 15% of the gross income under the 1954 Code.

Notes (2) Gross income figures are either taken directly or derived from figures in the U. S. Bureau of Mines 1952 Minerals Yearbook—Vol. I.

Notes (3) Tax computed at the corporation rate of 52%.

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No. 220

JUL 22 1957

JOHN T. FEY, Clerk

In the Supreme Court of the United States

OCTOBER TERM, 1957

UNITED STATES OF AMERICA, ET AL., PETITIONERS

v.

MERRY BROTHERS BRICK AND TILE COMPANY, ET AL., RESPONDENTS

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR RESPONDENTS IN OPPOSITION

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No. 220

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v.

MERRY BROTHERS BRICK AND TILE COMPANY, ET AL., RESPONDENTS

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR RESPONDENTS IN OPPOSITION

This brief in opposition is filed on behalf of the respondents in the thirteen cases covered by the petition for a writ of certiorari.

Question Presented

The Government's statement of the question presented (Pet 2-3) is inaccurate and misleading. Under the Internal Revenue Code, taxpayers' percentage depletion deduction is to be computed as a percentage of "gross income from the property," which the Code

specifically defines as "gross income from mining." The Code[1] then specifically broadens the meaning of "mining" as generally understood:[2]

> "The term 'mining' *as used herein* shall be considered to include *not merely* the extraction of the ores or minerals from the ground *but also* the ordinary treatment processes normally applied by mine owners or operators in order to obtain the *commercially marketable mineral product or products* . . . " (Emphasis supplied.)[3]

The question presented is:

> Where taxpayers extract clay from their own deposits and process it into burnt clay products (such as brick and tile), and the undisputed facts show (1) that taxpayers' clay is not commercially marketable until put into the form of such burnt

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[1] Internal Revenue Code of 1939, Section 114(b)(4)(B), set forth in the petition, p. 43. The corresponding provision of the Internal Revenue Code of 1954, Section 613(c) (Pet. 47), is substantially the same.

[2] The basic fallacy in the Government's petition is its complete disregard of this language, wherein Congress has specifically and deliberately departed from and enlarged the meaning of "mining" ("business of making or of working mines") found in the dictionary. (See Webster's New International Dictionary, Unabridged (2d ed. 1953).

[3] The petition (pp. 2, 10, 19, 20) is replete with the suggestion that the decisions below allow a taxpayer to compute his depletion allowance on the sales price of a "manufactured" or "finished" product whenever "he chooses to combine [manufacturing] activities with his mining activities." (Pet. 19) This is simply not the case. Under the decisions below, the applicable percentage is applied to the

clay products, (2) that owners and operators of such clay deposits must normally process their clay into such burnt clay products in order to obtain products which they can market commercially, and (3) that the taxpayers' processes are the ordinary ones used to produce such products, are the processes which taxpayers thus apply included in the statutory term "mining".

Statement

The Statement in the petition (pp. 3-7) sets forth some of the facts involved in these cases. However, it omits any reference to the essential facts on which the decisions below are based, namely:[4]

(1) that the taxpayer's brick and tile clay is not commercially marketable until it is processed into burnt clay products (R. 62);

(2) that only negligible amounts of the brick and tile clay mined in the United States can be sold before it is processed into such products (R. 62); and

---

selling price of the first "commercially *marketable* mineral product", that is, the first product which is *marketable* in commerce, whether that is a "crude" product or a "manufactured" or "finished" product. If a taxpayer should choose to apply a process subsequent to those normally applied to obtain a *marketable* product, that process would not be "mining", because the product would be commercially *marketable* before it was applied.

[4] Record references are to the *Merry Brothers* case. The petition correctly states (p. 7) that, "The facts and issues in the remaining cases are in all material respects the same as in the *Merry* and *Reliance* cases."

(3) that taxpayer's processes are the ordinary treatment processes by which brick and tile clay generally is extracted from the ground and processed into such products, and are the processes normally employed by the industry (R. 59).

The District Court held that taxpayer's depletion deduction is to be computed on the selling price of its burnt brick and tile (R. 62), and the Court of Appeals affirmed. (Appendix, pp. 28-35)

Argument

A. *The petition presents no important question of federal law which needs to be settled by this Court.*

The sole question in these cases is one of statutory construction. The petition (p. 11) recognizes that this question has been decided against the Government by four Courts of Appeals (the First, Fourth, Fifth and Tenth Circuits).[5] These Courts, with fourteen circuit judges (including four chief judges) participating,

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[5] *United States* v. *Cherokee Brick & Tile Company*, 218 F. 2d 424 (5th Cir. 1955); *Townsend* v. *The Hitchcock Corporation*, 232 F. 2d 444 (4th Cir. 1956); *United States* v. *Sapulpa Brick & Tile Corporation*, 239 F. 2d 694 (10th Cir. 1956); *Dragon Cement Company, Inc.* v. *United States*, — F. 2d — (1st Cir. 1957); and the decision below, *United States* v. *Merry Brothers Brick & Tile Company*, 242 F. 2d 708 (5th Cir. 1957).

Judge Magruder's opinion in the *Dragon Cement* case, together with the opinion of the court below, is reproduced herein in the Appendix, pp. 13-35.

Taxpayers' position is also supported by the earlier case, not mentioned by the Government, of *New Idria Quicksilver Mining Co.* v. *Commissioner*, 144 F. 2d 918 (9th Cir. 1944).

have written five considered opinions, without a single dissent. There is no conflict among the circuits. In all five opinions, the Courts hold that the statutory language is "clear and unambiguous", and they are in complete agreement as to its meaning. They carefully consider and reject all arguments made by the Government.

The Government appealed the instant cases to the Fifth Circuit, which had previously decided the issue in *United States* v. *Cherokee Brick & Tile Company*, *supra*, note 5, and asked that Court to reconsider and overrule that decision. The cases were argued before three circuit judges, none of whom had participated in the *Cherokee* decision. The Fifth Circuit, upon "the fullest and most careful re-examination and reconsideration" of the *Cherokee* decision, reaffirmed it, "since the undisputed facts and every sound consideration of statutory construction and application support indeed compel the conclusion that it was right and should be adhered to." (Appendix, pp. 30-31)

Furthermore, with the single exception of one District Court decision which has now been reversed,[6] the numerous District Courts which have considered this question, as well as the Tax Court, have all decided it in exactly the same way.[7]

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[6] *Dragon Cement Company, Inc.* v. *United States*, 144 F. Supp. 188 (D. Me. 1956), reversed by the First Circuit; see note 5, *supra*. The reasoning of this District Court is so obviously erroneous that the Government does not even suggest it in its petition.

[7] In addition to the District Court decisions in the Fourth, Fifth and Tenth Circuits which have been affirmed by the respective Courts of Appeals, the issue has been decided

Faced with this array of adverse decisions, the Attorney General asks for a writ of certiorari, principally on the ground that the issue involves "hundreds of millions of dollars of revenue." (Pet. 8)[8] The fact that a large amount of revenue is involved does not mean, in the sense of Rule 19, that there is an "im-

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the same way by District Courts in the Sixth and Ninth Circuits. *The Haviland Clay Works Company* v. *United States*, 56-1 U.S.T.C. ¶ 9297, 1956 P.-H. Fed. Tax Service ¶ 72,449 (N.D. Ohio 1956); *Harvey* v. *United States*, 57-1 U.S.T.C. ¶ 9473, 1957 P.-H. Fed. Tax Service ¶ 72,532 (D. Ariz. 1957).

The Tax Court has consistently taken the same position. *International Talc Company*, 15 T.C. 981 (1950); *American Gilsonite Company*, 28 T.C. —, No. 22 (1957); *Riverton Lime & Stone Company, Inc.*, 28 T.C. —, No. 49 (1957).

[8] We question the accuracy of the estimates made in the petition (pp. 11-12) on the basis of the unverified, unsupported and unexplained data transmitted over the signature of the Acting Commissioner (Pet. 58-61), and we strenuously object to their inclusion, since they are not a part of the record in any of these cases. Since the dollar amount involved has no proper bearing on whether a writ of certiorari should be granted, there is no occasion to search out all the unjustified assumptions and errors infecting that material. It might be noted, however, that the Government's estimate completely ignores the statutory limitation of the depletion deduction to 50% of "net income from the property". It also assumes the lack of a market for all minerals listed in the Appendix, before they are processed into some "finished" product, although the applicability of the legal principle of these cases will depend entirely on the purely factual question of marketability. There is no basis, therefore, for the Government's assumption that this legal principle will cause a loss of revenue in the amounts estimated as to all those minerals. (Pet. 60-61)

portant question of federal law which has not been, but should be, settled by this court." Since the sole issue here has been carefully considered and settled by four different Courts of Appeals (which have not been kept in the dark as to the amounts of revenue involved), and since those courts unanimously agree that the statute is "clear and unambiguous," we submit that such issue is now so lacking in substance that it is not sufficiently "important" to warrant review by this Court, regardless of the amounts involved. In fact, there is no *real* question left.[9]

The complete unanimity among the Courts of Appeals on the present question of statutory construction is, we submit, a decisive reason for denial of certiorari. *If there can ever be a situation of any importance to the revenue where an issue is settled short of a decision by this Court, these cases present that situation.*

B. *The decisions below are clearly correct.*

In view of the unanimity of the Courts of Appeals, we submit that there is no occasion for this Court independently to consider the merits of the issue here involved in passing on the Government's petition. If, however, this Court should feel called upon to inquire into the merits, a reading of the *Dragon Cement* opinion and the opinion below will establish that the deci-

[9] Review by this Court certainly is not necessary in order to put an end to recurring litigation on this issue. Denial of certiorari here would undoubtedly cause the Government to conform its position to the overwhelming authority against it.

sions below are clearly correct.[10] These opinions conclusively show that the Government's arguments, both those here made and others now abandoned, are completely without merit under the statute and should be addressed, if at all, to Congress, not to the courts.[11]

While any argument on the merits here would be superfluous, we do feel that we should correct the Government's misstatements concerning the regulation here involved. The Government erroneously states that the portion of the regulation here involved is of long

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[10] In the Appendix, where these opinions are reproduced, those portions of the opinions relating particularly to the Government's arguments here are printed in bold type (pp. 18-19, 23, 25, 32-35).

[11] For example, the Government attempts to show that the statute, as applied by the courts below, "produces grave inequities within and among classes of taxpayers" and that these decisions will not give "a uniform application to a nationwide scheme of taxation". (Pet. 19, 20). The amount of depletion for various ores and minerals is clearly a matter for Congress to determine. Of course, under the statute there will be some variation among producers of the same mineral, due to differences in local prices, products produced, net income, royalties paid, etc. Such variations are inherent in percentage depletion as this Court stated in *Helvering* v. *Mountain Producers Corporation*, 303 U.S. 376, 381 (1938):

> "But to appraise the actual extent of depletion on the particular facts in relation to each taxpayer would give rise to problems of considerable perplexity and would create administrative difficulties which it was intended to overcome by laying down a simple rule which could be easily applied. To this end, the taxpayer was permitted to deduct a specified percentage of his gross income from the property. See *United States* v. *Dakota-Montana Oil Co.*, 288 U.S. 459, 461.

standing and constitutes a contemporaneous construction of the Statute. (Pet. pp. 9, 17-18.) The portion of the regulation on which the Government relies relates to situations where the mine owner applies processes *beyond* "ordinary treatment processes" and is not applicable here.[12] The validity of that portion of the regulation is not here involved. The portion of the regulation which has been held invalid by the courts below, that is, the portion which would exclude from "ordinary treatment processes" a number of the processes required to make brick and tile ~~clay~~, is not of long standing and does not constitute a contemporaneous construction of the statute; it was first promulgated on July 14, 1953, *almost ten years after the enactment* of Section 114(b)(4)(B).[13] It has no counterpart in any prior regulation.

Congress was free to give such an arbitrary allowance as the deduction was an act of grace. In answer to the contention that the provision may produce 'unjust and unequal results,' we have remarked that this is likely to be so 'wherever a rule of thumb is applied without a detailed examination of the facts affecting each taxpayer.' *Helvering* v. *Twin Bell Syndicate*, 293 U.S. 312, 321."

[12] That portion of Section 29.23(m)-1(f) of Treasury Regulation 111 on which the Government relies and which it quotes in the petition (p. 9, note 7) provides for computing "gross income from the property" in a case where the mine owner or operator processes an ore or mineral *beyond* "ordinary treatment processes". In view of the holding below that all of taxpayers' processes are "ordinary treatment processes", the quoted portion of the regulation is inapplicable here.

[13] This portion of Section 29.23(m)-1(f), added by T. D. 6031, C. B. 1953-2, 120 (Pet. 49 at 51), purports to interpret

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be denied.

Respectfully submitted.

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the statutory term "ordinary treatment processes" so as to exclude therefrom treatment effecting a chemical change, blending with other material, thermal action, fine pulverization, pressing into shape and molding.

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July, 1957

APPENDIX

Bold type in Appendix is supplied by Counsel, italics by the Courts

UNITED STATES COURT OF APPEALS FOR THE FIRST CIRCUIT

No. 5186

DRAGON CEMENT COMPANY, INC.,
Plaintiff, Appellant

v.

UNITED STATES OF AMERICA,
Defendant, Appellee

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF MAINE

[144 F. Supp. 188]

Before MAGRUDER, *Chief Judge*, and WOODBURY and HARTIGAN, *Circuit Judges*.

OPINION OF THE COURT

May 14, 1957

MAGRUDER, *Chief Judge*. Appellant, a Maine corporation, in its capacity as successor (by merger effective November 30, 1951) to Lawrence Portland Cement Company, a Pennsylvania corporation, brought this action in the United States District Court for the District of Maine, seeking recovery of federal income and excess profits taxes for the

period January 1 to November 30, 1951, in the amount of $483,522.19, with interest. The facts were not in dispute and were recited in a stipulation. Both parties having moved for summary judgment, the district court on September 24, 1956, entered a judgment the first paragraph of which (as subsequently amended) decreed that the plaintiff recover of the defendant the sum of $10,546.46, with interest, on account of a deductible tax loss under § 23(f) of the Internal Revenue Code of 1939, an issue which is no longer in the case, and the second paragraph of which decreed as follows:

> "2. That plaintiff take nothing further in consequence of plaintiff's complaint as to the issue of percentage depletion and as to that issue, the action be and it is hereby dismissed on the merits."

The taxpayer has appealed from that portion of the judgment denying recovery to it under the percentage depletion issue, so that the case now before us turns solely on a question of statutory interpretation of § 114(b)(4)(B) of the 1939 Code, as amended, which defines the term "gross income from mining" for use in determining the basis for percentage depletion allowed as a deduction from income derived from certain mines and natural mineral deposits.

The allowance for depletion has been a controversial subject for years, and officials of the executive branch have sought from time to time, with conspicuous lack of success, to persuade the Congress to eliminate some of its alleged overgenerous features. See Mertens, Law of Federal Income Taxation § 24.04 (1954). We are not concerned with the wisdom or policy of the statutory allowance, once we are sure what the allowance is, for it is plainly our judicial function merely to apply the allowance as Congress wrote it and meant it.

The need for and fairness of some allowance for depletion proceeds from the fact that the production of income through the exploitation of natural resources is accompanied by an inevitable consumption of capital in the form of the gradual exhaustion of the natural resource being exploited. Thus the allowance serves to offset the injustice of classifying only as income what might be regarded as income comingled with return of capital, and serves also as an incentive to encourage capital expenditures in the direction of discovery and exploitation of natural resources.

Of the three types of depletion allowance prescribed at various times by the Congress, percentage depletion (with which we are now concerned) is to be contrasted with cost depletion and discovery depletion. Cost depletion, based upon the cost to the taxpayer of the particular deposit, seeks to return to the taxpayer free of tax that portion of his cost attributable to the amount of the deposit used up in earning the income on which he is taxed during a given taxable year. Discovery depletion seeks to reward the taxpayer for the discovery of unknown natural deposits, and has usually been based upon the fair market value of the deposit within thirty days after the date of its discovery. By the third type of depletion allowance, percentage depletion, the Congress hoped to furnish an easily computable allowance that would avoid many of the complications arising in connection with the computation of cost or discovery depletion. Percentage depletion is based upon a fixed percentage of the income realized during the taxable year from the exploitation of a piece of property—the percentage varying, somewhat arbitrarily, depending upon the kind of deposit involved.

With the gradual enlargement of the categories of mineral properties to which the percentage depletion became applicable, the Congress has at the same time automatically

eliminated discovery depletion in respect to such deposits.[1] In general, percentage depletion has remained as an alternative to cost depletion, so that even if the taxpayer fails to establish the cost of the property, he nevertheless may be entitled to the allowance of a percentage depletion. It is also true, as pointed out in Mertens, Law of Federal Income Taxation § 24.31a (1954), "that through percentage depletion a taxpayer may recover more than his cost over the life of the property."

For present purposes we need go no further back than to the provisions of the Internal Revenue Code of 1939.

Section 23 of this Code contained the following (53 Stat. 12, 14):

> "Sec. 23. Deductions from Gross Income.
>
> In computing net income there shall be allowed as deductions: . . .
>
> (m) Depletion.—In the case of mines, oil and gas wells, other natural deposits, and timber, a reasonable allowance for depletion and for depreciation of improvements, according to the peculiar conditions in each case; such reasonable allowance in all cases to be made under rules and regulations to be prescribed by the Commissioner, with the approval of the Secretary. . . .
>
> (n) Basis for Depreciation and Depletion.—The basis upon which depletion, exhaustion, wear and tear, and obsolescence are to be allowed in respect of any property shall be as provided in section 114."

Section 114(b)(1) stated as the general rule (53 Stat. 45) that the basis for the depletion allowance should be the adjusted basis in § 113(b) for determining gain upon

[1] The 1954 Code has now abolished discovery depletion entirely as applied to future years.

the sale or other disposition of such property, except as otherwise provided in the ensuing paragraphs numbered (2), (3), and (4). Paragraph (2) related to discovery value in the case of certain mines. Paragraph (3) gave a percentage depletion formula for oil and gas wells. Paragraph (4) gave percentage depletion formulas for coal, metal, and sulphur mines (but not including the type of deposit involved in the case at bar), and provided allowances based upon a prescribed percentage of the "gross income from the property during the taxable year".

The phrase "gross income from the property" was undefined as it appeared in the 1939 Code. It thus had a lurking ambiguity where the mine owner customarily performed more than merely extractive operations before realizing any income; in such cases, would the basis for the depletion allowance include gross income from what in other contexts might be described as manufacturing operations upon the extracted property? The statute did not make this point clear, and Regulations 111, as originally issued, naturally sought to narrow the scope of the allowance.

In the Revenue Act of 1943 (58 Stat. 43), the Congress attempted to resolve this ambiguity by inserting a definition of "gross income from the property" in a new § 114 (b)(4)(B), reading in part as follows:

> "(B) Definition of Gross Income From Property.—As used in this paragraph the term 'gross income from the property' means the gross income from mining. The term 'mining', as used herein, shall be considered to include not merely the extraction of the ores or minerals from the ground but also the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products. The

term 'ordinary treatment processes', as used herein, shall include the following: (i) In the case of coal—cleaning, breaking, sizing, and loading for shipment; (ii) in the case of sulphur—pumping to vats, cooling, breaking, and loading for shipment; (iii) in the case of iron ore, bauxite, ball and sagger clay, rock asphalt, and minerals which are customarily sold in the form of a crude mineral product—sorting, concentrating, and sintering to bring to shipping grade and form, and loading for shipment; and (iv) in the case of lead, zinc, copper, gold, silver, or fluorspar ores, potash, and ores which are not customarily sold in the form of the crude mineral product—crushing, grinding, and beneficiation by concentration (gravity, flotation, amalgamation, electrostatic, or magnetic), cyanidation, leading, crystallization, precipitation (but not including as an ordinary treatment process electrolytic deposition, roasting, thermal or electric smelting, or refining), or by substantially equivalent processes or combination of processes used in the separation or extraction of the product or products from the ore, including the furnacing of quicksilver ores."

It is apparent that the Congress intended not to limit the computation of the percentage depletion allowance to the gross income attributable to purely extractive processes, for the deposit when thus first extracted might not be in a commercially marketable form, and might require further processing. Congress accomplished this by providing for the first time a general formula, and by giving nonexclusive illustrations of processes included in the phrase "ordinary treatment processes". See § 3797(b) of the Code of 1939, 53 Stat. 470. The general formula, which of course is controlling, is that the basis for computing the percentage depletion allowance shall be the

"gross income from mining", defined as including "not merely the extraction of the ores or minerals from the ground but also the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products." Thus we must look to see what processing is normally undertaken by a mine owner or operator in order to obtain a commercially marketable product, and when such a salable product is obtained, then the gross income from the sale of such product is the base upon which to apply the percentage depletion allowance. That these "ordinary treatment processes" are not necessarily limited to those processes which leave the extracted deposit in its natural state is clear from the inclusion, as an illustration in § 114(b)(4)(B), of the process of furnacing quicksilver ores, which involves a chemical change.

It would also be helpful, in a preliminary way, to observe that the depletion allowance is not an allowance upon any *process*, whether a mining process or a manufacuring process. Nor is it an allowance, as such, upon any product. Instead, it is an allowance to the mine owner designed as a simple means to diminish his taxable income from the exploitation of a natural resource which is necessarily exhausted in the process. In making this allowance, the Congress has elected not to limit the deduction in all cases to the taxpayer's actual cost or other basis in the land from which the ore or mineral is extracted. To supply a simpler rule, the Congress has turned more and more to the method of percentage depletion, which differs from both cost and discovery value depletion in that it is measured by an arbitrary percentage of gross income from the property, without regard to the taxpayer's cost or discovery value.

From the foregoing it is clear that by the enactment of 1943 the Congress for the first time introduced into the

statute key language which had not theretofore appeared either in the statute or in the regulations thereunder, namely, a new definition of "gross income from mining" as including "not merely the extraction of the ores or minerals from the ground but also the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products." Notwithstanding this, the Commissioner has subsequently sought, by regulatory amendments to § 29.23(m)-1(f) of Treas. Reg. 111, in cases where the mine owner customarily had to indulge in further processing other than merely extractive operations before obtaining a commercially marketable product upon which he could realize any income, to prescribe a relatively complex mathematical method for calculating the percentage depletion base. This would require an allocation of income derived from the sale of the first marketable product to the various treatment processes in proportion to their cost, with only those processes allowed as part of the base which occurred before any chemical change had taken place in the extracted mineral.

By § 319 of the Revenue Act of 1951 (65 Stat. 497), the Congress amended § 114(b)(4)(A) of the Internal Revenue Code so as to extend the availability of percentage depletion for the first time to "calcium carbonates," which includes deposits of cement rock, the natural resource involved in the case at bar. The prescribed percentage for calcium carbonates was ten per cent of the gross income from mining the deposit.

With the foregoing stated by way of background, it will perhaps be easier to understand the significance of the facts in the present case.

Throughout the tax period in question, Lawrence Portland Cement Company, the taxpayer-appellant's predeces-

sor, owned and operated two quarries, one in Maine and the other in Pennsylvania, from which it extracted cement rock, a calcium carbonate suitable for conversion into cement. The operations began with drilling and primary blasting from the face of the quarry by the open pit method to obtain the cement rock, which was then broken into manageable size by secondary blasting and loaded by shovels into dump trucks which carried it to an inclined railway where it was deposited into dump rail cars for transportation to the near-by plant.

Treatment or "beneficiation" then occurred at the plant in the following processes: The dump rail cars deposited the cement rock into a large primary crusher, which reduced the size of the extracted rock to pieces with a maximum dimension of about eight inches. After this primary crushing, the cement rock fell onto a conveyor belt which carried it to a secondary crusher which further reduced the size of the rock. From the secondary crusher a conveyor belt carried the cement rock to a shed, from which it was picked up by an overhead crane which deposited the desired quantities into a hopper, over which a coarse bar grate was fitted to screen the crushed cement rock. From the hopper, the screened cement rock was gravity fed to a ball mill where it was ground with water to a proper fineness known as "slurry," which was then conveyed to a wet "slurry" tank where it was kept in suspension by a revolving paddle mechanism. The "slurry" was then run off to filters where much of the water was removed, and the resulting filter cake was thereafter conveyed by belt to rotary kilns.

There is no dispute that the gross income allocable to the operations thus far described may be included in determining the gross income from mining of the mineral, cement rock, for the purpose of calculating the base to

which the allowable percentage depletion is to be applied. But it was found as a fact by the trial court, and we understand that this is not controverted by the government, that except in negligible amounts, which may be disregarded, "there is no commercial market for cement rock. The first commercially marketable product is cement. The methods used by taxpayer to transform cement rock into cement are admitted to be the 'ordinary treatment processes normally applied by mine owners or operators' who produce cement."

Accordingly, the taxpayer's predecessor had to engage in further processes before obtaining a marketable product, cement, upon which gross income could be realized. The so-called filter cake was run into the upper end of rotary kilns, which were in the form of long rotating cylinders set at a slight inclination, the filter cake gradually traveling toward the lower end of the kiln. Hot gases from a flame at the lower end evaporated the water from the filter cake and burned the remaining material to a dense clinker. The clinker was then conveyed to a grinding mill where it was ground to the fineness of cement; the cement was finally placed in silos from which it was loaded and shipped in bags or in bulk. It is conceded that these last processes effected a chemical change in the cement rock, transforming it from its crude mineral state into cement, which is synthetic and not a mineral.

The dispute here involves the propriety of including income allocable to the kiln and post-kiln processes in gross income from mining, as defined; if such processes are excluded, the depletion allowance for the taxable period would be $204,859.19, whereas, if such processes are included, the allowable depletion would be $795,852.60.

It is contended by the government that mining terminated, and that the depletion base was arrived at, when the mine operator had prepared the cement rock for conver-

sion, and that the subsequent operations, during which it underwent a chemical change and ceased to be a mineral, constituted a manufacturing process, not allowable in computing the depletion base. As indicated above, this contention is fully supported by Treas. Reg. 111, § 29.23(m)-1(f), but the taxpayer maintains that the regulation is invalid in this respect because the definition of "gross income from mining", inserted in § 114(b)(4)(B) in 1943, does not permit such an interpretation, but on the contrary compels the opposite result. Although the district court upheld the government's view, we find ourselves in agreement with the taxpayer.

Preliminary to upholding the government's asserted interpretation, the district court concluded that the statutory language, "commercially marketable mineral product or products", was intrinsically ambiguous. One possibility, the district court said, was to construe the phrase as permitting the depletion allowance to extend to a product of a mineral, although the end product may be a synthetic nonmineral (*viz.*, a commercially marketable mineral *product*). The second possibility, said the district court, was to construe the statutory phrase as restricting the depletion allowance to products still in a mineral state (*viz.*, a commercially marketable *mineral* product).

We are unable to perceive that the statutory language contains any such inherent ambiguity. In this connection it should be observed that three other courts of appeals which have had occasion to weigh the government's arguments advanced in the case at bar, and to construe the critical statutory phrase, have held it to be "clear and unambiguous" in favor of the taxpayer's interpretation. See *United States* v. *Cherokee Brick & Tile Co.*, 218 F. 2d 424, 425 (C.A. 5th, 1955); *Townsend* v. *The Hitchcock Corp.*, 232 F. 2d 444, 446 (C.A. 4th, 1956); *United States* v. *Sapulpa Brick & Tile Corp.*, 239 F. 2d 694, 697 (C.A. 10th,

1956). We are not persuaded that we ought to create a conflict with our brethren in other courts of appeals with respect to this matter.

In the first place it should be noted that cement has been consistently classified as a "mineral product" both in scholarly compilations of a general sort, such as the Encyclopedia Britannica,[2] and in publications of specialized government agencies which compile information and statistics on the mining industry. Such classification has been made by the Bureau of Mines and the Bureau of the Census, both of which had listed cement as a "mineral product" at the time the statutory definition of "gross income from property" was enacted in the Revenue Act of 1943,[3] and this classification has been continued in the latest publications of these agencies.[4]

Furthermore, it is well known that the word "mineral" is frequently used before other words to describe products which are manufactured from minerals but which are not themselves composed of minerals in the natural state. In such usage it qualifies the noun which follows and indicates mineral origin; for example, "mineral wool" is a generic term which can be applied to various insulation products manufactured from minerals.[5] The dictionary furnishes many similar examples.[6]

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[2] 22 Encyc. Britannica 753, Table XIII (1954).

[3] Minerals Yearbook for 1942, pp. 38, 45, 48 (1943); Statistical Abstract of the United States, 1942, p. 845. In addition, the Statistical Abstract statistics as to production of cement (pp. 879, 888) appear in a section entitled "Mining and Mineral Products."

[4] Minerals Yearbook for 1953, vol. 1, p. 20 (1956); Statistical Abstract of the United States, 1956, pp. 732, 743.

[5] 9 Kirk & Othmer, Encyc. of Chemical Technology 122 (1952).

[6] *E. g.*, *mineral oil*, "Any oil of mineral origin, as petroleum, shale oil, or any oil *obtained from them by refining*"; *mineral water*, "Any water naturally or *artificially* impregnated with mineral salts.

The legislative history of § 114(b)(4)(B) provides additional support for the interpretation of the statutory definition which we, along with other courts of appeals, have adopted. In order to support its conclusion that cement is not a "mineral product" within the meaning of the statutory definition, the district court seized upon the word "mineral" as the crucial word in the phrase "the commercially marketable mineral product or products." However, that "mineral" is not the crucial word is made clear by the Senate Finance Committee Report which explained the meaning of the section added by that committee to the Revenue Act of 1943:

> "The purpose of the provision is to make certain that the ordinary treatment processes which a mine operator would normally apply to obtain a *marketable product* should be considered as a part of the mining operation, and to give reasonable specification of what are to be considered such processes for various kinds or classes of mines. (Underscoring added.) Sen. Rep. No. 627, 78th Cong., 1st Sess., 23, 1944 Cum. Bull. 991.

In other words, although the draft of the bill to which the above report referred contained the word "mineral" and the phrase was in the same form as in the final Act, the committee did not even use the word "mineral" in explaining that the purpose of the statutory provision was to make certain that the ordinary treatment processes which a mine operator would normally apply to obtain a marketable

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or gases"; *mineral jelly*, a "semisolid substance *from petroleum* . . . used as a stabilizer in explosives"; *mineral spirits*, a "volatile petroleum product, intermediate between gasoline and kerosene, used extensively as a thinner for paints and varnishes"; *mineral rubber*, which includes "an asphalt *artificially* obtained or treated." (Italics added.) Webster's New International Dictionary, Unabridged (2d ed. 1953).

product should be considered as a part of the mining operation, as defined.

Nor can we accept the government's contention that the Congress in 1943 was concerned solely with making clear that concentration processes, equivalent to those which had previously been listed in the applicable regulations, were intended to be included as a part of the mining operation, for in defining "gross income from mining" the Congress introduced new language which had never previously appeared in the history of the depletion allowance. Furthermore, the Senate Finance Committee Report which explained the provision gave no hint that Congress intended only to include such "equivalent concentration processes". Quite the contrary, as the previous quotation shows, the committee report stated that the purpose of the new provision was "to make certain that the ordinary treatment processes which a mine operator would normally apply to obtain a marketable product should be considered as a part of the mining operation".[7]

For the reasons above indicated, we conclude that the taxpayer is entitled to a percentage depletion deduction based upon its gross income from cement, as the first commercially marketable mineral product obtained from the deposit, calcium carbonate, after the ordinary treatment processes normally applied by such mine owners. To the extent that § 29.23(m)-1(f) of Treas. Reg. 111 is inconsistent with this conclusion, it must be declared to be invalid.

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[7] It should also be observed that the government's position is subject to the anomaly that under its interpretation there never is a "commercially marketable mineral product" obtained from cement rock. Thus, to be perfectly consistent, "mining" under § 114 (b) (4) (B) would not include any "ordinary treatment processes" applied to cement rock, since mining includes only "ordinary treatment processes" applied to obtain the "commercially marketable product or products."

See *Manhattan General Equipment Co. v. Commissioner*, 297 U.S. 129, 134 (1936).

A judgment will be entered vacating that portion of the judgment of the District Court now under review, and remanding the case to the District Court for further proceedings not inconsistent with this opinion.

IN THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

No. 16373

UNITED STATES OF AMERICA,

Appellant.

versus

MERRY BROTHERS BRICK AND TILE COMPANY,

Appellee.

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF GEORGIA

No. 16323

UNITED STATES OF AMERICA,

Appellant.

versus

RELIANCE CLAY PRODUCTS COMPANY,

Appellee.

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF TEXAS

March 27, 1957

Before HUTCHESON, *Chief Judge*, and RIVES and BROWN, *Circuit Judges*.

HUTCHESON, Chief Judge:

These appeals from judgments of the United States District Court for the Southern and Northern Districts of Georgia[1] and Texas,[2] respectively, involve claims for re-

[1] Dated July 3, 1956, opinion reported 145 F. Supp. 186.

[2] Dated May 14, 1956; no written opinion.

fund of income and excess profits taxes. They present on the same basic facts the same basic question, and have therefore been submitted and argued together.

This question is whether this court will depart from its decision in *U. S.* v. *Cherokee Brick & Tile Co.*, 218 F(2) 424, in which, affirming the judgment and approving the opinion of the United States District Court for the Middle District of Georgia, in *Cherokee Brick & Tile Co.* v. *United States*, 122 F. Supp. 59, we said, at pages 424-25, of the pertinent portion of Sec. 114[3] of the Internal Revenue Code:

> "The statutory language is clear and unambiguous, which is that gross income from mining must include the income from ordinary treatment processes which must be applied to the ore or mineral in order to obtain the commercially marketable mineral product, that is, the first product which is marketable in commerce. There is no provision in the statute for excluding any process before such a marketable product is reached. The only restriction is that the processes must be the ordinary treatment processes normally applied by mine owners or operators."

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[3] "(b) Basis for depletion.

* * * * * * *

"(4) (A) The allowance for depletion under Sec. 23(m) in the case of the following mines and other natural deposits shall be—

"(i) in the case of * * * brick and tile clay * * * 5 per centum. * * * of the gross income from the property during the taxable year. * * *

"(B) Definition of gross income from property. As used in this paragraph the term 'gross income from the property' means the gross income from mining. The term 'mining' as used herein shall be considered to include not merely the extraction of the ores or minerals from the ground but also the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products. * * *"

> "The complaint alleges that, of the brick and tile clay mined in the United States, there is opportunity for the sale of only a negligible quantity before it is put into the form of burnt brick and tile. This allegation is admitted in the answer of the appellant. For this and other reasons (but mainly for this one) stated in the opinion of the district court, above cited, the judgment appealed from should be affirmed."

Conceding that the cases were decided below in accordance with our decision in the *Cherokee* case and that if that decision stands, they must be affirmed, the United States, stating: "Since this decision, the United States District Court of Maine, in *Dragon Cement Co. v. United States*, 144 F. Supp. 188", has, declining to follow the *Cherokee* decision, put forward an interpretation of its own of the statute, goes on to say:

> "In view of this interpretation and the great number of decisions which have arisen within this circuit following the decision in *Cherokee Brick & Tile Co.*, and which involve substantial amounts of revenue, the government respectfully asks this court to reconsider its decision."

Pointing out that, with the exception of that in the *Dragon* case, all of the numerous decisions in the district courts in this and other circuits and of the Courts of Appeals for the Fourth Circuit, in *Townsend v. The Hitchcock Corp.*, 232 F(2) 445, and the Tenth Circuit, in *U. S. v. Sapulpa Brick & Tile Co.*, . . . F(2) . . . , have agreed with and approved our decision, appellees insist that the grounds now put forward in support of its reconsideration present no sound reasons therefor.

They urge upon us moreover that if we should enter upon such a reconsideration of the decision, the result would only be to reaffirm it, since the undisputed facts and every sound consideration of statutory construction and

application support indeed compel the conclusion that it was right and should be adhered to.

Upon the fullest and most careful re-examination and reconsideration of our decision in the *Cherokee* case, in the light of the records and the briefs and arguments in that case and these, we agree that this is so. Because it is and because in their decisions the district court and this court dealt adequately and correctly with the question presented in it and here, we will not undertake to restate or further elaborate upon the reasons they gave but will content ourselves with saying that, upon the plain and simple consideration set down and for the reasons pointed up in the *Cherokee* case, we decline to depart from the decision in it, and, on its authority, affirm the judgments appealed from.

We think it not amiss, however, to say that we have taken particular note of and approve the comment in appellee Reliance Clay Products Company's brief.[4] We have

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[4] "As one of the principal reasons for asking this Honorable Court to overrule the Cherokee case, the Government cites a District Court decision from the District of Maine, Dragon Cement Co. v. United States, 144 F. Supp. 188, a case involving cement rock. The Court there held that the cement which the taxpayer sold was not the 'commercially marketable mineral product' within the meaning of Section 114 (b) (4) (B), although it was shown that only negligible quantities of cement rock could be sold before it was put in the form of cement.

"The Court reached this conclusion by a curious process of reasoning. It stated that cement is not a 'mineral product' within the statute, because chemical reactions in the kiln change the cement rock into a 'synthetic product'. The Court held that 'the emphasis must here be upon the word "mineral" as a noun', and that, therefore, a 'mineral product' is a product 'still in a mineral state.'

"The Court thus rewrote the statute to refer to the 'commercially marketable mineral', rather than the 'commercially marketable mineral product or products.' *Furthermore, it ignored completely the fact that Congress intended Section 114 (b) (4) (B) to provide*

also taken particular note of and agree with Proposition No. 2 in Merry Brothers' brief, "*The government's attack on the* Cherokee *case is based on the fallacious assumption that the* Cherokee *decision allows depletion on 'manufacturing processes'*" (emphasis supplied), and its argument thereunder reproduced in part in the margin,[5] as well

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a simple marketable product rule to obtain the starting point for the computation of the percentage depletion deduction. The Court in the Dragon Cement case recognized that, under its interpretation of 'mineral product', there never is a 'commercially marketable mineral product' obtained from cement rock. Thus the decision in the Dragon Cement case completely frustrates the purpose of Congress to provide the marketable product rule for computing the depletion deduction for all ores and minerals granted percentage depletion by Section 114 (b) (4), including cement rock and brick and tile clay. * * *

"The Court in the Dragon Cement case ignored the plain, obvious and generally understood meaning of 'mineral product' as will be shown below. It seized upon the word 'mineral' as the crucial word in the statutory phrase 'the commercially marketable mineral product or products.' That the word 'mineral' is not the crucial word in the statutory phrase is made clear by the Senate Finance Committee Report, quoted above, explaining the meaning of Sec. 114 (b) (4) (B), which that Committee added to the Revenue Act of 1943:

> "The purpose of the provision is to make certain that the ordinary treatment processes which a mine operator would normally apply to obtain a *marketable product* should be considered as a part of the mining operation. * * *" (emphasis supplied) Sen. Rep. 627, 78th Cong., 1st Sess. p. 23.

"*Although the draft of the bill to which this Report referred contained the word 'mineral' and the phrase was worded exactly the same as it was in the final Act, the Committee did not even mention the word 'mineral' in explaining that the purpose of the provision is to enable the mine operator to obtain a 'marketable product.'*" (emphasis supplied)

[5] "The Government's basic argument is not related to the language of the statute, but rests rather upon the theory or 'concept' of depletion which, the Government asserts, Congress had in mind when it granted the deduction. The Government argues, basically, that in the light of the theory of depletion it is unreasonable to

as its corrollary "*that the Government's argument ignores the obvious fact that Congress intended Sec. 114 (b)(4) to provide a simple, practical rule which could easily be applied to compute the percentage depletion deduction*" (emphasis supplied) and its argument in support repro. duced in part here:

> "* * * **we might also point out here that the Government's argument completely ignores the obvious fact that Congress intended Sec. 114(b)(4) to provide a simple, practical rule which could be easily applied to compute the percentage depletion deduction.**

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suppose that Congress would have provided a deduction based on the gross income from the sale of 'manufactured' or 'finished' products such as brick and tile. The Government's brief undertakes to confuse the issue by giving the impression that the statute allows depletion on 'mining' or 'mining processes' and that this Court in the Cherokee case sustained a deduction for depletion not only on 'mining processes' but on 'manufacturing processes' or on a 'manufactured product'.

"Nothing could be further from the truth. Depletion is 'not allowed on any process, 'mining' or 'manufacturer', and is not allowed on any product. It is just as absurd to talk of allowing depletion 'on' the first 'mining' process of extracting clay from the ground, as it is to talk of allowing depletion 'on' the last 'manufacturing' process of burning the clay in the kiln. On the contrary, depletion is allowed to compensate the miner owner for exhaustion of his natural deposit. But instead of limiting the depletion deduction to a recovery of the cost of the natural deposit, Congress has chosen to allow the deduction to be computed as a stated percentage of the selling price of the 'commercially marketable mineral product', the selling price of the mineral product for which a commercial market exists. It has done so by defining 'gross income from the property' in Sec. 114 (b) (4) (B) to include not only the income derived from the extraction process but also the income from processes applied to the ore or mineral, after extraction from the natural deposit, to obtain the commercially marketable mineral product. But in no sense does this mean that depletion is allowed 'on' any of the processes or 'on' the products produced thereby, or that such processes or products are 'depleted'. We feel that this simple analysis disposes of the Government's whole argument."

"In order to compute a percentage depletion deduction, there must be a dollar base to which to apply the applicable percentage. Congress elected to use the marketable product rule as a simple means to provide this dollar base. With this dollar base established in Subparagraph (B) of Section 114(b)(4), Congress can then set the applicable rates in Subparagraph (A) to produce the dollar amount of depletion which it wishes to grant in the case of each particular type of natural deposit without disturbing the simple means for determining the dollar base. Of course, the processing necessary to obtain marketable products from the ores and minerals mined from the various types of natural deposits will vary greatly, but this fact can be taken into account in fixing the applicable rates. Thus, Congress has set rates in Sec. 114(b)(4)(A) which vary from 5% to 23%, and these rates can be raised or lowered as Congress sees fit.

"* * * If Congress upon further consideration should feel that applying the applicable rate to the gross income from any product, whether or not it is a 'manufactured' product, produces too large a depletion deduction, and should wish to decrease that deduction, it has only to lower the rate while still using as a base the gross income from the marketable product.

"In spite of its effort to conceal the fact, the Government's argument in sum and substance is merely that 5% of the selling price of burnt brick and tile is too large a deduction to allow the mine owner as compensation for that part of the brick and tile clay deposit consumed in producing that brick and tile. However, the amount of the deduction to be allowed to the miners of brick and tile clay is a matter exclusively for Congress. The Government, therefore, recognizing that it cannot ask this court to change the rate of 5%

specified in the statute for brick and tile clay, seeks instead to have this court rewrite the statute by changing the dollar base to which the rate is applied, as the court did in the Dragon Cement case."

The judgments are AFFIRMED.

(6032-7)